




THE BULGARIAN ECONOMY

IN THE FOURTH QUARTER OF 2002

THE BULGARIAN ECONOMY

IN 2002 (SUMMARY)

REPORT BY
**THE CENTER
FOR ECONOMIC
DEVELOPMENT**



The Center for Economic Development (CED) is a Bulgarian non-governmental research institute in the area of economic policy, established in 1997. Its goal is to support the economic development of Bulgaria through encouragement of public debate on economic issues and development of economic policy options.

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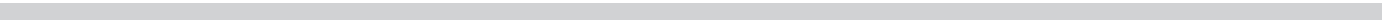
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ABBREVIATIONS USED

AD (JSC)	JOINT STOCK COMPANY
APC	ACT ON THE PROTECTION OF COMPETITION
ATPSME	ACT ON THE TRANSFORMATION AND PRIVATIZATION OF STATE-OWNED AND MUNICIPAL ENTERPRISES
BAAT	BULGARIAN AGENCY FOR ALTERNATIVE TOURISM
BDU	BULGARIAN DOCTORS UNION
BIBA	BULGARIAN INTERNATIONAL BUSINESS ASSOCIATION
BNB	BULGARIAN NATIONAL BANK
BTC	BULGARIAN TELECOMMUNICATIONS COMPANY
CC	COMMERCIAL CODE
CEFTA	CENTRAL EUROPEAN FREE TRADE ASSOCIATION
CITA	CORPORATE INCOME TAX ACT
CITUB	CONFEDERATION OF INDEPENDENT TRADE UNIONS IN BULGARIA
CoM	COUNCIL OF MINISTERS
EA	EMPLOYMENT AGENCY
EAD (SPJSC)	SOLE PROPRIETORSHIP JOINT STOCK COMPANY
EBRD	EUROPEAN BANK FOR RECONSTRUCTION AND DEVELOPMENT
EC	EUROPEAN COMMISSION
EFTA	EUROPEAN FREE TRADE ASSOCIATION
EU	EUROPEAN UNION
G&S	GOODS AND SERVICES
GDP	GROSS DOMESTIC PRODUCT
GFCF	GROSS FIXED CAPITAL FORMATION
GS	GOVERNMENT SECURITIES
GVA	GROSS VALUE ADDED
HPP	HYDRO-POWER PLANT
ICT	INFORMATION AND COMMUNICATIONS TECHNOLOGIES
IMF	INTERNATIONAL MONETARY FUND
LFS	LABOR FORCE SURVEY
LTFA	LOCAL TAXES AND FEES ACT
MAF	MINISTRY OF AGRICULTURE AND FORESTS
MEW	MINISTRY OF ENVIRONMENT AND WATER
MLSP	MINISTRY OF LABOR AND SOCIAL POLICY
MoE	MINISTRY OF ECONOMY
MoF	MINISTRY OF FINANCE
MoI	MINISTRY OF THE INTERIOR
MSSC	MANDATORY SOCIAL SECURITY CODE
NAMRB	NATIONAL ASSOCIATION OF MUNICIPALITIES IN THE REPUBLIC OF BULGARIA
NEC	NATIONAL ELECTRIC COMPANY
NFA	NATIONAL FRAMEWORK AGREEMENT
NHIF	NATIONAL HEALTH INSURANCE FUND
NMSS	NATIONAL MOVEMENT SIMEON THE SECOND
NPITA	NATURAL PERSONS INCOME TAXATION ACT
NSI	NATIONAL STATISTICAL INSTITUTE
NSSI	NATIONAL SOCIAL SECURITY INSTITUTE
OECD	ORGANIZATION FOR ECONOMIC COOPERATION AND DEVELOPMENT
OPEC	ORGANIZATION OF PETROLEUM EXPORTING COUNTRIES
OPF	OCCUPATIONAL PENSION FUND
PA	PRIVATIZATION AGENCY
PIC	PENSION INSURANCE COMPANY
PPA	PUBLIC PROCUREMENT ACT
PPCA	PRIVATIZATION AND POST-PRIVATIZATION CONTROL ACT
SAC	SUPREME ADMINISTRATIVE COURT
SERC	STATE ENERGY REGULATION COMMISSION
SME	SMALL AND MEDIUM-SIZED ENTERPRISES
SPF	SUPPLEMENTARY PENSION FUND
SSS	STATE SOCIAL SECURITY
TPS	THERMAL POWER STATION
UDF	UNITED DEMOCRATIC FORCES
UNO	UNITED NATIONS ORGANIZATION
UPF	UNIVERSAL PENSION FUND
VAT	VALUE ADDED TAX
VATA	VALUE ADDED TAX ACT
VPF	VOLUNTARY PENSION FUND
WTO	WORLD TRADE ORGANIZATION

PART ONE

THE BULGARIAN ECONOMY IN THE FOURTH QUARTER OF 2002

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The Bulgarian economy during the fourth quarter of 2002 preserves its growth. Macroeconomic stability persists; growth is mostly determined by industrial sales and output. Labor market dynamics, certain growth of real income according to household budgets statistics, proceeds in tourism, capital market indicators, and the progress of the negotiations for accession to the European Union can also be given positive assessment.

At the same time, many aspects of economic dynamics and economic policy constitute issues of concern and so is the condition of business environment. A relative growth of foreign investments compared to the previous months was observed in the last quarter of 2002, but volumes remain at lower levels. The trade deficit for the quarter under review, taken on an annual basis, registers a serious negative trend. Shocks in the judiciary system are accompanied by lack of noticeable progress in key areas such as healthcare reform, elimination of administrative barriers, and other components of business environment. The Estat Index of business climate in Bulgaria registers a stable downward trend.

Business climate in Bulgaria is evaluated employing the summarized estimate by the representatives of nearly 400 interviewed Bulgarian enterprises. The latest survey was conducted in early January. **The Estat Index of business climate** integrated estimate for the last quarter of 2002 is -2.55. The registered drop expressed as an absolute value is insignificant (-0.71 percentage points) and the index remains within the neutral portion of the scale, which interprets the business climate as "neither favorable, nor unfavorable". Nevertheless, the Estat Index registers a stable downward trend, which indicates gradual change for the worse of the business climate in Bulgaria. The fourth quarter of 2002 does not register any material change in entrepreneurs' assessment of general business environment, but the conclusion about the neutral character of this environment is generally confirmed. Some indicators reveal a more favorable opinion of the business compared to the previous quarters. This is most clearly observed with respect to questions about the tax environment - the trend of a more positive attitude towards the tax policy is preserved in the last quarter. The somewhat better assessments of entrepreneurs about the conditions for start up of new business and about administrative barriers are another positive aspect. The business gives more negative assessments of some indicators concerning important components of business environment - the judiciary, protection of intellectual property, policy for promotion of innovations. Indicators such as quality and efficiency of Government administration, changes of legislation and consistency of Government legislative initiative, practical implementation of regulations, stability and reliability of the banking system did not register any material change in the fourth quarter.

The combination of shortage of resources and funds and unstable economic and political environment is the major factor for the growing pessimism about business development in a short-term and long-term perspective. The business environment remains unstable. The low return on investments and the fear of bankruptcy block the willingness of owners to invest in the core business or in some other activity. According to company managers, Government policy does not encourage business development and does not contribute to a stable economic environment.

However, according to **NSI's general business climate indicator** the fourth quarter of 2002 is characterized by a slightly more favorable economic situation compared to the previous quarter and to the fourth quarter of 2001. The industrial business climate indicator remained at approximately the same levels as in the previous quarter. In the construction sector the indicator registers the highest levels compared to the corresponding quarters of previous years, although they are lower in a seasonal aspect compared to most of the other months of 2002. In the fourth quarter of 2002 the business climate in retail trade improved compared to the same quarter of the previous year, but still remained below the levels of this indicator for the corresponding quarters of the period 1997-2000, and also below the long-term average.

GDP growth in the fourth quarter of 2002 is not expected to be lower than the growth in the fourth quarter of 2001 (4.2 per cent), mainly as a result of the higher monthly growth, taken on an annual basis, of sales in industry and trade, and mostly of industrial output. GDP growth in the third quarter (4.5 per cent) and for the first nine months of 2002 (4.4 per cent) confirms former expectations that Bulgarian economy continues to develop at comparatively high pace.

In the fourth quarter of 2002 monthly **inflation rate** is less than 1.2 per cent and is mainly a result of higher food prices compared to the previous month. But in the quarter under review food prices are lower compared to the average prices for this group for the whole 2001. In the fourth quarter of 2002 the increase of consumer prices, taken on an annual basis, is more moderate compared to the increase in the corresponding months of 2001. A possible military operation in Iraq will be the major pro-inflation factor in the next months.

In the fourth quarter of 2002 the number of registered **unemployed** marked accelerated decrease (by about 20 thousand people in November and December compared to the previous month). The difference between the number of registered unemployed and the number of people who define themselves as unemployed is preserved - in December the number of registered unemployed increased by around 60 thousand people. Hidden employment has been partly confirmed by the first results of a large-scale joint examination conducted

by the National Social Security Institute and the Employment Agency. Results show that around 27 thousand people are registered both with the National Social Security Institute as employed and with the Employment Agency as unemployed. In the fourth quarter of 2002 the basic characteristics of the labor market improved compared to the corresponding period of the previous year. According to data from NSI's Labor Force Monitoring, in the fourth quarter of 2002 the seasonal decline of the number of economically active people remains of the order characteristic for the previous year (around 140 thousand people), but a structural improvement is observed - the number of unemployed registers a decrease (by 40 thousand people), and not an increase.

Overall, the execution of the 2002 **consolidated fiscal program** is successful. The execution of the revenue part corresponds to the adopted program. **Revenues** up to December 2002 amount to BGN 12 525 m., or 100.9 per cent of the program. **Expenditures** amount to BGN 12 743 m., or 100.6 per cent of the program. A **deficit** to the amount of BGN 218 m. is registered.

As of end of December 2002 the total amount of **government and government guaranteed debt** was BGN 18 180 m., or 56 per cent of the Gross Domestic Product (according to updated estimates of the latter by the Ministry of Finance). Compared to the end of the third quarter, the total amount of debt is decreased by BGN 748 m., mainly as a result of a negligible decrease of the debt denominated in US Dollars, which was accompanied, however, by material depreciation of the dollar compared to the Euro, according to measurements as of end of the two periods. But the dollar equivalent of the total amount of government and government guaranteed debt increased by USD 102 m from end of September till end of December 2002. Along with the appreciated Euro compared to the dollar, this is also due to the changed foreign currency structure of the debt. The latter fact is explainable rather by the positive net foreign financing than by the September restructuring of the foreign debt accounted in the last quarter of 2002. As of end of September 2002 the debt denominated in US Dollars amounted to 51.60 per cent of total government and government guaranteed debt, whereas at end of December the debt denominated in US Dollars amounted to 49.79 per cent.

Total amount of **foreign debt** increased by USD 12.6 m. from end of September till end of December. However, in the period under review the debt denominated in BGN decreased by BGN 816 m. as a result of the appreciated Euro. According to end of December estimates, total amount of foreign debt is USD 8 524.6 m. or BGN 16 069 m. According to data of the Ministry of Finance, as at end of December total **domestic debt** amounted to BGN 2 111.7 m. (including government debt of BGN 2 109.8 m. and internal government guarantees of BGN 1.9 m.). Total amount of domestic debt increased by BGN 82.1 m. compared to the end of the third quarter of 2002.

In the fourth quarter of 2002 the pace of **privatization** in the state sector remains unsatisfactory in terms of both proceeds and the number of transactions made. Only 16 companies where the State holds the majority interest and 12 detached parts were sold. Government's intentions to accelerate the privatization process, to intensify the activity on the capital market by offering shares of big and attractive companies, and to liquidate the minority stakes of the State in more than 1350 companies, were not fulfilled. Government's expectations to finalize the two biggest privatization transactions - for BTC EAD and Bulgartabac - Holding AD, did not come true. With a 2002 annual plan of 664 privatization transactions, including sale of 238 companies where the State holds the majority interest, as of 31 December 2002 the number of privatization transactions made was only 275, according to data by PA. The annual plan is fulfilled at 41.4 per cent. The number of enterprises with majority interest sold is 73 (the annual plan for these companies is fulfilled at 31 per cent). That influenced the overall execution of the revenue part of the Annual Privatization Plan.

In the beginning of October the Vice-Premier and Minister of Economy introduced in the National Assembly a package of measures to improve the business environment and promote the economy till mid 2003. One of the adopted measures included lowering the minimum threshold of VAT registration to BGN 50 thousand, which would enable small and medium-sized businesses to get tax credit in 2003. Thereby the preferential treatment of the big business is partially eliminated and an opportunity for registration of some small and medium-sized companies under VATA is provided. As from 2003 e-Government and the "one-stop shop" administrative service are expected to facilitate citizens and the business in making use of Government administration services. Access to financing remains a serious barrier to the development of Bulgarian small and medium-sized companies. A positive sign in this field is the more intensive competition of commercial banks which penetrate the sector of lending to Bulgarian small and medium-sized businesses. The 2002 Regular Report of the European Commission on the progress of Bulgaria, which was published in October, states that "Bulgarian policy for small and medium-sized enterprises largely conforms to the principles and goals of EU's policy in respect of enterprises, but the lack of resources and coordination, as well as the ambiguous perspectives of the institutional organization in the SME field, have limited the efficient implementation of the policy for SMEs". Further efforts to improve the awareness of enterprises about the changes undertaken by the Government in the field of commercial and tax legislation are recommended.

The persisting trend of parallel growth of export and import is a major characteristic of **foreign trade** in the fourth quarter of 2002. The weak growth of world economy and the low demand on international markets did not prevent the further growth of Bulgarian export, which reached USD 1 414.1 m. (estimated). Export to CEFTA countries registers the highest growth (by

nearly 30 per cent), but EU countries remain a major partner, accounting for 55.6 per cent of total exports. Two points are worth noting in terms of export commodity structure: export of investment goods (mainly machinery and equipment) takes the lead with an increase of 29.3 per cent, and Bulgarian food products restore their positions in exports, registering an increase of over 28 per cent. Imports (CIF) increased by around 20 per cent compared to the same period of 2001 and amount to USD 2339.8 m. (estimate), with 80 per cent going for industrial consumption (mainly for production of export goods). The balance of trade deficit (calculated on the basis of FOB export and CIF import) amounts to USD 925.7 m., registering an increase of around 40 per cent compared to the last quarter of 2001.

The inflow of **foreign investments in Bulgaria** is in line with the current situation on international financial markets, which is characterized by general uncertainty and delay of investment projects on account of war prospects and the low growth rates of world economy. Besides, scandals around the new Privatization Act prevented the realization of the big privatization transactions planned. Thus, total investments for the last quarter of 2002 are estimated at USD 203.2 m. They register considerable increase compared to the third quarter and a negligible decrease compared to the fourth quarter of 2001, accounting for 44 per cent of total investments for the year (USD 458 m.).

The political debate about the future of Kozloduy NPP in connection with Bulgaria's position in the negotiations with the European Union dominated the government policy in the **energy sector**. Bulgarian Government's decision to close down units 3 and 4 by the end of 2006 enabled to close Chapter 14: Energy of the negotiations for accession. At the same time this position generated internal political tension, which gave grounds to a group of MPs to attack the position in court. Along with that, a peer review of the condition of the two units was negotiated. At the end of the quarter under review Bulgaria decommissioned units 1 and 2 of Kozloduy NPP, in accordance with the 1999 arrangements with the European Union. The close down of these two units will not have any effect on electricity prices, on the capacity of the national energy system to meet local demand, and on the level of unemployment in the region of Kozloduy in the short and medium term.

Prices of oil products got stabilized at higher levels and followed an upward trend. Increase was somewhat restrained by the dollar depreciation compared to the lev. Higher price levels have unfavorable effect on the energy intensive Bulgarian economy, which was most felt in the chemical and the transport sector. Notwithstanding the higher crude oil prices at international markets, the State Energy Regulatory Commission did not change the prices at which Bulgargas is selling natural gas on the domestic market. This decision is rather favorable for the Bulgarian economy because natural

gas costs of big consumers will not increase.

The adjudicated bankruptcy of Balkan Airways and the set up of Balkan Air Tour as the new national air carrier were the highlights of **transport sector** development in the quarter under review. The objective of Government's intervention in the air transport sector was to keep Bulgaria's positions on the civil aviation market. The successful fulfillment of this objective is not guaranteed yet, regardless of the fact that the State ensured good starting positions for the new national air carrier.

The approved (though with a great delay) Bulgarian e-Government Strategy is an important event in the sector of **high technology and communications**. The document is only the starting point of a long and complex process, which is expected to result in e-Administrative services for Bulgarians in a couple of years. The last quarter of 2002 also brought a long-awaited and desired change concerning nearly all Bulgarian ICT consumers - as of January 2003 the depreciation rate of computers, software and software right of use is 50 per cent taken on an annual basis, which is much closer to the actual depreciation time of such assets. This will enable companies to update their computers and software at shorter intervals, which will make them more competitive on international and local markets.

In the last quarter of 2002 tourism preserved its good pace of development. Proceeds from **tourism** amount to USD 183.4 m., with USD 151.1 m. for the same period of the previous year. In the fourth quarter of 2002 the balance of tourist services amounted to USD 41.6 m. (USD 23 m. for the last quarter of 2001). The above data justify the optimistic expectations for a successful winter season. Some projects declared or launched at the end of the previous year also support the above findings. Their objective is to improve the conditions in winter resorts (general and special infrastructure) and to extend the skiing season. The new Tourism Act took effect. It regulates in detail the relationship between tourists and tour operators or tour agents. It also simplifies the licensing regime - hotel- and restaurant-keeping licenses are eliminated, but tour operator and tour agent licenses are preserved. A couple of regulations to the act also took effect - Regulation on Categorization and Regulation on the Licensing of Tour Operators and Tour Agents, as well as the Tariff of Charges Collected under the Tourism Act. Categorization requirements for tourist sites are increased. A decision to set up an Executive Agency for National Tourism Promotion and Information as a legal person financed from the budget was taken in the fourth quarter of 2002.

There was a speed up of the work on harmonization of legislation in the field of **agriculture** in fulfillment of the task to accelerate negotiations for accession to EU. The amendments to the Farmers Support Act, which regulates government support to farmers, and the implementation of the measures incorporated in the National Plan for Development

of Agriculture and Rural Areas are the most important points. This act also approved the functions of the State Agricultural Fund: to provide financial support to farmers; to intervene on the markets of agricultural products; to subsidize export, and to provide management of the SAPARD Program. The Act on the Census of Bulgarian Farms, which sets forth 1 July 2003 as a starting date of the census, is of paramount importance for the process of negotiations on Chapter Agriculture. The amount, scope, and orientation of direct subsidies and payments in the agrarian sector to be allocated for Bulgaria after its accession to EU will be dependable on that.

Positive trends in the **capital market**, observed throughout the whole 2002, were preserved in the last quarter of the year – stock exchange trade in compensatory instruments, which started in September, remained at high levels, the SOFIX index registered an upward trend, market capitalization also increased notably in the third quarter. All that, along with the higher liquidity of some securities, particularly those covered by the index, is also accepted as a sign of improvement of public companies' indicators, improved corporate governance, or at least as market adjustment of the prices of Bulgarian securities, which have been undervalued for years. Nevertheless, the role of the capital market in the financial sector of Bulgaria remains generally insignificant – as of end of December 2002 the total market capitalization of the Bulgarian Stock Exchange Sofia - AD was slightly above 4 per cent of the updated projection (MF estimate) of GDP for 2002. The underdeveloped capital market is explainable by the general condition and future trends of Bulgarian economy, as well as by the fact that the financing mechanisms of this alternative non-bank environment remain unfamiliar or unpreferred even when corresponding projects were available. Liquidity remains at low levels, the market does not encourage good corporate governance, and investment alternatives remain limited.

Financial intermediation is still provided mostly through the **banking system**. The condition of banks in Bulgaria remains stable, with excellent measures of capital adequacy and liquidity, and well-functioning banking supervision. Overall, in the last quarter of 2002 the banking system registered further increase of assets and deposits, as well as of current profit. Loans to the non-government sector manifest a clear upward trend. The higher level of loans to households in 2002 is definitely a signal of retail banking development. Notwithstanding the objective indicators of a stable upward trend of lending activity, general assessments indicate underutilized potential for lending, including in support of small and medium-sized enterprises, and for diversification. The banking system of Bulgaria remains stable but insignificant in terms of the amount of assets and the share of provided loans in GDP.

Discussions in the **social security** sector were focused on the measures to be implemented by MLSP since the beginning of 2003 to increase the collection rate of social security

contributions and to decrease the share of gray economy, including introduction of minimum social security thresholds by economic activities and sectors and mandatory registration of labor contracts at the NSSI. The new Social Security Code, which provides for implementation of above measures as of the beginning of 2003, was passed at first reading in December 2002. Two thirds of the minimum social security thresholds were agreed between employers and trade unions, and the other one third was determined by expert evaluation with the participation of representatives of employers, trade unions, and the Government. NSSI is of the opinion that the minimum social security thresholds reflect the real condition of the labor market in terms of labor force demand and supply. The effect of the new social security policies is estimated at approximately BGN 162 m., however variations are possible, which generates risks for the 2003 NSSI budget. Start of negotiations to define minimum salaries and wages by sectors and professions is expected in 2003.

The downward trend of the number of registered **unemployed** was preserved in the fourth quarter of 2002. Registered unemployed decrease in number with every month, although effects are not quite notable yet. In November the number dropped for the first time below the limit of 17 per cent of the economically active population. The downward trend of unemployment is in harmony with the employment growth processes registered in the regular labor force monitorings conducted by NSSI. Decrease of unemployment is a result of the subsidized employment measures developed and implemented by MLSP and of the abated negative effects of economic restructuring and liquidation of loss-making companies. The list of specific employment programs proposed by the Ministry of Labor and Social Policy and implemented in cooperation with municipalities and employers is continuously expanded and updated in accordance with pilot phase results. Lower tension on the labor market is also a result of economic growth.

Another important aspect of Government's policy to reduce unemployment is the application of **incentives to promote employment**. Implementation of these incentives on a larger scale is expected in 2003. With that end in view, amendments to the Corporate Income Taxation Act and the Employment Promotion Act were adopted at the end of 2002.

The upward trend of nominal and real **incomes** of the population, established by household budgets statistics, was confirmed in the last three months of 2002. It is also accompanied by higher trust of consumers, with balance and expectations for the next 12 months definitely positive for all questions in the survey: financial situation of households, inflation, and unemployment.

An important change in the social policy of this Government was regulated in the fourth quarter of 2002: a differentiated

approach of **social assistance** was introduced, which resulted in more efficient distribution of resources towards the most underprivileged groups (single old people above the age of 75, disabled people, single parents). By way of an amendment to the Regulation on the Application of the Social Assistance Act, whereby higher and differentiated coefficients are introduced, in 2003 more than 100 000 underprivileged people will get higher social benefits.

In the last quarter of 2002 discussions on the **healthcare reform** were focused on the Act on the 2003 Budget of the National Health Insurance Fund, on the amendments to the Health Insurance Act, and on the Human Medications and Pharmacies Act. The 2003 National Framework Agreement was not signed by the end of 2002. By way of the recent amendments to the Health Insurance Act, the Government actually secured for itself the right to make arrangements and decisions, leaving to NHIF's management implementation only. The Government quota in the Fund's Assembly of Representatives was increased to 18 people against 6 people each for employers, the insured persons, and municipalities. In contrast to the practice of previous years, in 2003 NHIF's expenditures on certain items are fixed, and reallocation of funds to cover possible shortages under other items is not allowed. According to the amendments to the Health Insurance Act, the minimum amount of capital of a health insurance company is required to have to apply for a license is BGN 500 000, with the company undertaking to increase its capital to BGN 2 million within 3 years after it has been licensed. The objective is to enable more private health insurance companies to enter the market of private healthcare services, with a view to increase the competition on this market of healthcare services. The objective of the strategy for restructuring of Bulgarian in-patient care, approved by the Government in mid October 2002, is to improve the efficiency of in-patient care in conformity with affordability, timeliness, sufficiency and quality requirements. An Action Plan to the Strategy for the period up to 2007 was also approved. In the last quarter of 2002 the Minister of Healthcare issued two ordinances whereby the basic package of healthcare services to be covered from NHIF's budget and the list of diseases for which NHIF will cover in full or in part the medications for out-patient treatment, were approved.

The last quarter of 2002 was indicative of future priorities of Government's **environmental policy**. Against the background of a general positive assessment of the negotiation process on Chapter Environment, the European Commission confirms in the 2002 Regular Report the considerable progress Bulgaria has made in incorporating the Acquis in national environmental legislation. Along with that, the Report focuses on the need to integrate environmental policy in the other sector policies (particularly those for agriculture, energy, and transport) and to implement efficient measures for environment protection and use of natural resources. The quarter under review can be characterized as a period of intensive dialogue between

Government authorities, the Ministry of Environment and Water in the first place, and municipal structures on the implementation of infrastructure projects targeting environmental problems of individual regions. Intensified Government interest towards the results of currently implemented environmental management programs of enterprises reveals that a model of constructive business - executive power dialogue is possible. International financial aid and Bulgaria's active participation in many bilateral and multilateral environmental projects and programs are positive factors promoting this cooperation.

The period October - December 2002 is characterized by important to Bulgaria decisions and events in the area of **negotiations for accession to the EU**. By closing temporarily Chapter 14: Energy, Bulgaria proceeded to a new phase of the negotiations for membership. Temporary closed chapters are 23, another seven are to be closed by the end of negotiations. The 2002 Regular Report of the Commission on the Progress of Bulgaria was published a few days later, on 9 October 2002. It is stated for the first time that Bulgaria is a functioning market economy. The 2001 assessment classified Bulgaria as a country close to the functioning market economy. In the meantime the foreign ministers of EU Member States adopted a decision that Bulgaria and Romania would not take part in the 2004 European parliamentary elections and would lose their places set forth in the Nice Agreement. These two deputy quotas will be now distributed among the ten countries of the first wave. The European Council in Copenhagen (12-13 December 2002) adopted important to Bulgaria decisions. Bulgaria and Romania will become EU members in 2007, provided that they continue their progress in fulfilling membership criteria. The Danish Presidency wanted to secure EU enlargement after 2004, when the union will comprise 25 states, by engaging the countries of the first wave with the membership of Bulgaria, Romania, and Turkey.

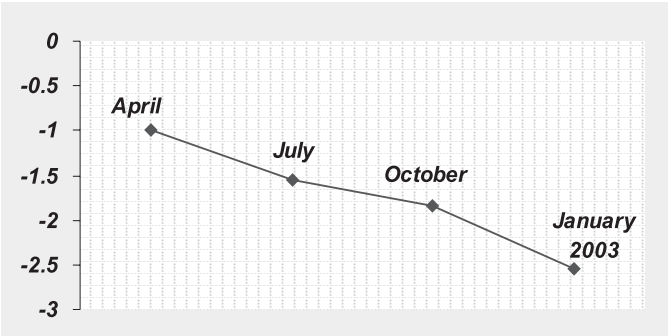
The development of Bulgarian economy in the fourth quarter of 2002 was also accompanied by certain changes in **other components of business environment**. Efforts to improve the business environment and promote economic growth were manifested in the package of 9 legislative and structural measures involving the set up of a Government Investment Fund, creating industrial zones, reform of the Commercial Code in the part concerning bankruptcy and liquidation, solving the problem of inter-company indebtedness, development of capital markets, creating a real estate market index, eliminating and simplifying licensing and registration regimes, enhancing the role of the Bulgarian Agency for Export Insurance, and other tax and social measures, which was announced in October. There was also progress in the work on development and adoption of some important laws to facilitate the conditions for doing business. The Parliament passed on first reading an Act on Economic Activity - Related Regulations and Administrative Procedures. The special work group at the Council of Ministers continued its work on development of new amendments to

the Public Procurement Act to be adopted in 2003. A draft on amendments to the Commercial Code in the part concerning bankruptcy and liquidation has been developed with a view to introduce quick and efficient procedures in this field. In the fourth quarter of 2002 the judicial system witnessed severe shocks, disputes and contradictions, which confirmed the need of radical reforms in this sector. Corruption remains a serious problem, which impedes business activity. Implemented measures do not yield still expected definite and clear results. This is probably one of the reasons for the president's proposal to set up a special anti-corruption body equally independent from all institutions. In December the Government adopted a Concept to Improve One-Stop-Shop Services and an e-Government Strategy. The objective of these documents is to facilitate people, the business, and Government administration; to reduce the sources of corruption; to save time and money.

The Estat Index of Business Climate

The Estat Index integrated estimate¹ for the last quarter of 2002 is **-2.55**. The registered drop expressed in absolute terms is insignificant (-0.71 percentage points) and the index remains within the neutral part of the scale, which interprets the business climate as “neither favorable, nor unfavorable”. Nevertheless, the Estat Index manifests a stable downward trend, which indicates gradual change for the worse of the business climate in the country (Figure 1).

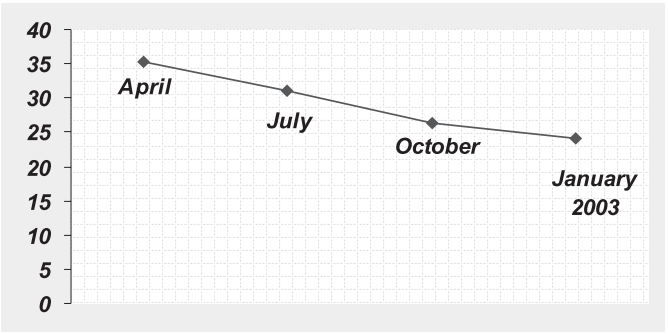
Figure 1. Business Climate Dynamics



Concerns about the economic situation are caused by changes in the investment attitude of managers; lower estimate of the general condition of economic actors; lower labor market potential; growing discontent with the Government policy concerning the business.

The Estat Index Component II values reveal a continuing drop in the propensity of Bulgarian companies to invest. The trend registered in the previous surveys is preserved. With such dynamics, the value may well move from the positive (+20 to +60) to the neutral section of the scale (+20 to -20) (Figure 2).

Figure 2. Investment Attitude Dynamics



The changes occurring in the behavior and intentions of owners are indicated by the growing unwillingness on one part to invest their excessive funds in another activity - a drop from 54 per cent in April 2002 to 42 per cent in the beginning of January 2003, and on the other part to take a bank loan to invest - a drop from 68 per cent in April to 56 per cent in January. This is probably due to the unwillingness to take unnecessary risks,

which could jeopardize their survival on the market.

The share of company managers who think that they have partners on whom their business is dependable in a long-term perspective also dropped down by 10 per cent. This fact reveals the inability to develop strategies for longer periods due to the uncertainty and the impossibility to clearly forecast possible future situations, threats and opportunities facing the company.

The survey also reveals a certain change for the worse of the situation at the labor market, which is an indirect cause for the business' uncertainty about investments. The share of interviewed who agree that “they could easily find the workers and employees they need” has dropped down by over 12 percentage points (since July 2002).

The assessment of the snapshot condition and the real opportunities in the short-term and long-term is directly connected with the investment intentions of Bulgarian company managers (Figures 3 and 4).

Figure 3. Assessment of the current state of businesses

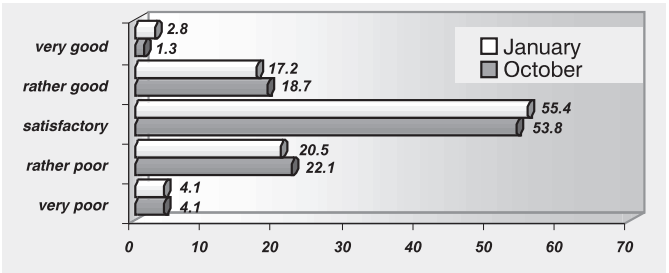
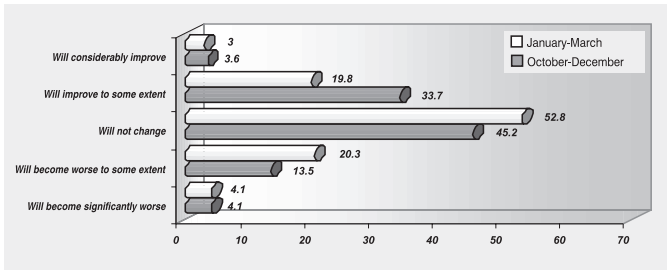


Figure 4. Expectations about the state of businesses in the next quarter



Survey results reveal that the business is seriously shaken in its opinion and does not have very optimistic expectations about the next quarter. On the contrary, there is a serious drop of over 15 percentage points in the share of the interviewed who believe that the condition of their business will improve in the next months. The fact that over 1/3 of the managers are of

¹ The index methodology and the mathematical model are developed by the Estat Agency for Social and Market Studies. The integrated indicator comprises three components. Component I “General Condition of the Company”, Component II “Investment Attitudes and Corporate Strategies”, and Component III “Business Environment”. The survey was conducted between 6th and 10th January 2003 and involved 399 companies. The sample is representative at the level of going concerns. Selection criteria for sample companies involve: region, sector, number of employees, and type of ownership. The scale employed to interpret the index is with a range of -100 up to +100 points and is divided in five equal ranges. Ranges thus defined practically exclude transferability from one category to another on the basis of random factors. The first, second and third Estat Index values fell within the “neutral” -20 +20 range.

the opinion that the company they manage does not have any competitive advantage over other companies in the relevant sector is another proof of the change for the worse in the real sector (Table 1).

Table 1. Position of companies compared to competitors, %

NUMBER OF COMPETITIVE ADVANTAGES	2002			2003
	April	July	October	January
none	19.5	28.3	32.5	33.1
1	19.8	13.1	16.3	17.0
2	18.8	24.2	17.6	18.3
3	16.5	14.4	13.9	12.0
4	13.2	7.8	10.8	10.3
5	7.1	6.9	3.7	4.0
6	5.1	5.3	5.2	5.3

The condition of big companies with more than 100 employees is interesting (Table 2). With sufficient human resources and equipment available, these should have considerable advantages over their competitors, however, the managers of 40 per cent of such companies state that they do not have any advantage. Yet, at the same time it is big companies again (24 per cent) that state 5 or 6 advantages which place them ahead of the other companies in the sector. This can be interpreted from the point of view of the fact that notwithstanding the real opportunities resulting from the available material resources and human capital, big companies are affected by the economic crisis or by pessimism.

Special attention should be devoted to micro-companies with less than 10 employees. Almost 1/3 of these do not have advantages over their competitors; only 6 per cent assess the position of their company as better compared to other companies.

Table 2. Competitive advantages profile by number of employees, %

NUMBER OF EMPLOYEES	NUMBER OF COMPETITIVE ADVANTAGES				TOTAL
	none	1 to 2	3 to 4	5 to 6	
up to 10	31.5	38.2	24.1	6.2	100.0
11 to 50	34.2	34.2	19.3	1.3	100.0
51 to 100	35.3	29.4	23.5	1.8	100.0
more than 100	40.0	16.0	20.0	24.0	100.0

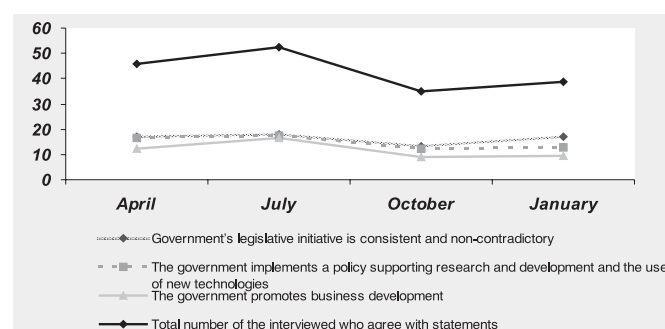
The apparent absence of competitive advantages is a result of the unstable business environment on one part and the shortage of resources on the other part. The low self-assessment of available material and financial resources characteristic of the previous months is preserved. There is lack of key resources for development such as new technologies (46 per cent), Internet (45 per cent) and information resources (32 per cent).

Business Environment According to Estat Agency

Surveys

The critical attitude of the business towards the Government for failure to support business development, to implement policies in support to research and development and the use of new technologies, for inconsistent and contradictory legislative activity, expressed as early as April of last year, becomes even more acute. This is a result of the aggravated situation in the sector and is among the major reasons for the lower propensity to invest (Figure 5).

Figure 5. Attitude towards the Government (share of the interviewed who agree with the statements)



Complaints about legislation, administration and existing corruption expressed in the previous months also persist in the beginning of 2003. However, the changes in the tax system concerning the patent tax also influence entrepreneurs' opinion about the bearability of this burden. The share of businessmen who think that "The patent tax is unbearable" dropped down from 57 per cent in April 2002 to 50 per cent in the first month of the new year.

No significant changes in entrepreneurs' assessment of the general business environment were observed in the fourth quarter. The conclusion about the neutral character of this environment is confirmed. Some indicators reveal a more favorable opinion of the business compared to the first quarter of the previous year.

This is most clearly observed with respect to questions about the tax environment - the trend of a more positive attitude towards the tax policy is preserved in the last quarter. Patent tax, social security and health insurance contributions, tax rates are given more positive assessment. In January 2003 seventy one per cent of the interviewed thought that these generated tax evasion, whereas in the first quarter of the previous year 80 per cent of the interviewed were of this opinion. The same could also be said about the profit tax rate in particular. In January 2003 thirty two per cent of the companies considered it bearable, whereas in April 2002 (the month of the first Estat Agency survey) 27 per cent of the respondents were of this opinion. Fifteen per cent of the interviewed now think that the tax system creates equal conditions for all companies, whereas

at the time of the first survey 10 per cent of the companies supported this statement.

Consequently, one of the conclusions that can be made from the analyses of the data from the last survey is that there is a positive trend in respect of the tax environment. Tax policy changes could be an explanation - stating in advance intentions in this field, which enables the business to better forecast and plan its activity and the necessary expenditures to cover its tax obligations towards the State.

The somewhat better assessments of entrepreneurs about the conditions for start up of new business, and about administrative barriers are another positive aspect. In principle, this is a field where the attitude of the business is strongly negative. Yet, at the same time 88 per cent of the interviewed in the latest survey thought that it was very difficult to start up a business, whereas in the beginning of the previous year 92 per cent of the interviewed were of this opinion. The same can also be said about administrative barriers - 77 per cent now believe that these constitute a major obstacle, whereas 80 per cent supported this opinion before. Measures taken in this field, particularly the "one-stop shop service" introduced in many Bulgarian municipalities, have a positive effect on this process and contribute to its considerable improvement.

The far more positive assessments of the business about the role of European integration constitute a fact that is also worth noting. On the face of it the change in the last quarter seems considerable - in the third quarter 47 per cent of the interviewed thought that harmonization of legislation will considerably improve the conditions for doing business in the country, whereas in the last quarter the percentage reached 54 per cent. Nevertheless, the value of this indicator remains rather low and there is a definite need to expand the campaign of informing the business about the progress of this process and the benefits it generates.

The business gives somewhat more negative assessments of some indicators concerning important elements of the business environment - the judiciary, protection of intellectual property, policy for promotion of innovations, etc.

On the whole, the opinion of entrepreneurs about the Government policy for business promotion is negative - only 9 per cent of the interviewed in the latest survey see such a priority outlined in the Government policy, whereas in the beginning of the year 12 per cent of the respondents were optimistic in this respect. A similar drop is observed in the assessments of the business about the policy for promotion of research and development and the use of new technologies. Assessments of the business about the judiciary remain strongly negative - 12 per cent of the interviewed in the first quarter of the previous year believed in the objectivity and efficiency of this system in the settlement of commercial disputes, and the percentage

is preserved in the latest survey. Unfortunately, despite the amendments to the Public Procurement Act, the assessment of public procurement assignment and implementation procedures remains strongly negative - only 8 per cent of the interviewed think that these procedures are objective and transparent (10 per cent were of this opinion in the beginning of the previous year). Protection of intellectual property is also called in question in the latest survey - it is efficient according to 15 per cent of the interviewed, whereas in the beginning of the previous year 18 per cent of the interviewed were of this opinion.

Indicators such as quality and efficiency of public administration, changes of legislation and consistency of Government legislative initiative, practical implementation of regulations, stability and reliability of the banking system remained almost unchanged in the fourth quarter.

Finally, the following conclusion could be drawn. The combination of shortage of resources and funds and unstable economic and political environment is the major factor for the growing pessimism about the business development in the short-term and long-term. The business environment remains unstable. The low return on investments and the fear of bankruptcy block the willingness of owners to invest in the core business or in some other activity. According to company managers, Government policy does not encourage business development and does not contribute to a stable economic environment.

NSI's Business Surveys

General business climate indicator²

The fourth quarter of 2002 is characterized by a slightly more favorable economic situation compared to the previous quarter and to the fourth quarter of 2001. Changes in the levels of the general business climate indicator are small compared to the previous month (no change in October, an increase of 1.5 percentage points in November and a decrease of 2.6 percentage points in December), with the indicator's value remaining comparatively high above its long-term average.

² NSI conducts business surveys in accordance with the harmonized EU program. Answers to the questions in the surveys are presented on a three-range category scale of the type: "increase", "no change", "decrease", or "above the normal", "normal", "below the normal". Balances of estimates are calculated as a difference between the relative shares of the extreme variants of an answer. The business climate indicator is a geometrical mean of the balances of estimates for the current business situation and the expected business situation of enterprises in the next 6 months. The general business climate indicator is a weighted arithmetical average of four branch business climate indicators: those of industry, construction, retail trade, and services - as of January 2003 NSI started to present the general business climate indicator including the business climate indicator values in the services sector available since May 2002.

Figure 6. Business Climate - total (NSI)

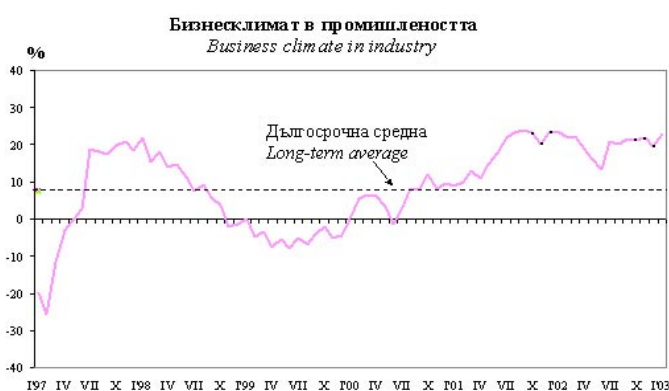


Source: NSI

Industry

In the fourth quarter of the year the industrial business climate indicator remained at approximately the same levels as in the previous quarter. For the fourth quarter NSI's business survey registers the highest for the year (but lower compared to the corresponding quarter of 2001) levels of current production activity in the industry sector. The highest level of current production activity in the industry sector for the year was registered in November, but in the same month economic managers lowered their expectations about the business in the next three months, and a comparatively sharp decline of current production activity was registered as early as December, with a holdback in the estimates of order levels both in the country and from abroad.

Figure 7. Business climate in industry (NSI)



Source: NSI

Construction

In the fourth quarter the "business climate in construction" and "current construction activity" indicators have in general the highest levels compared to the corresponding quarters of previous years and are above the long-term average, although they are lower in a seasonal aspect compared to most of the other months of 2002.

Figure 8. Business climate in construction (NSI)



Source: NSI

Retail trade

In the fourth quarter of 2002 the business climate in retail trade improved compared to the same quarter of the previous year, but still remained below the levels of this indicator for the corresponding quarters of the period 1997-2000, and also below the long-term average. The fluctuating improvement observed in the period January - September 2002, in parallel with a subsequent improvement of the retail traders financial performance indicator registered a change for the worse in October. By the end of the year the financial performance indicator almost restored its September level, but the business climate indicator did not register improvement mainly as a result of the more pessimistic expectations of traders for the next months.

Figure 9. Business climate in retail trade (NSI)



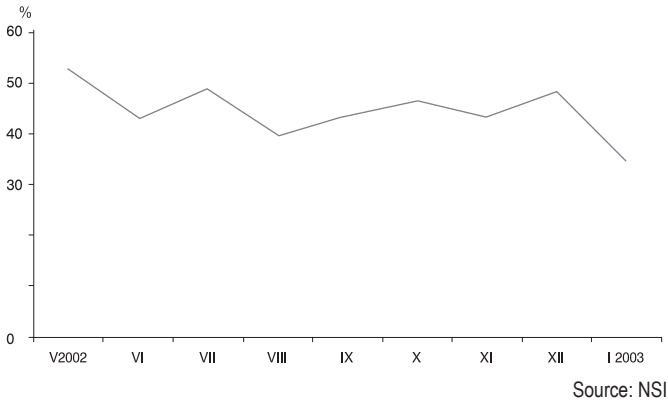
Source: NSI

Services (trade excluded)

Since May 2002 NSI conducts a monthly harmonized business survey in the service sector. The May and June business climate levels were positive, in July and August the indicator registered a decrease, in September and October it marked an improvement, in November it was more unfavorable compared to a month ago, and in December the business climate was more favorable compared to November only in the services

sector (an increase of 4.8 percentage points). Assessments of economic managers about demand improved. According to managers the economic environment is less uncertain, they have less financial problems, but at the same time enterprises have greater problems related to competition and economic legislation.

Figure 10. Business climate in service sector (NSI)



Gross Domestic Product

GDP growth in the fourth quarter of 2002 is not expected to be lower than the growth in the fourth quarter of 2001 (4.2 per cent), mainly as a result of the higher monthly growth, taken on an annual basis, of sales in industry and trade, and mostly of industrial production.

Table 3. Volume index, corresponding month of the previous year = 100, %

	Oct., 2002	Nov., 2002	Dec., 2002
Industrial production			
2002	100.6	111.0	100.8
2001	99.3	101.3	95
Industrial sales			
2002	97.1	103.8	102.1
2001	96.7	92.8	92.7
Domestic trade and repairing activities, total, net sales			
2002	109.5	109	111.1
2001	95.6	96.4	98.8
Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net sales			
2002	102.9	105.3	104.7
2001	95.9	104.8	101.8
Wholesale trade, net sales			
2002	111.6	110.8	113.4
2001	93.9	93.7	97.2
Retail trade, repair of personal and household goods, net sales			
2002	103.7	103.3	104.9
2001	103.1	103.5	103.0

Source: NSI

Data about GDP in the third quarter and in the first nine months of 2002 confirm former expectations that Bulgarian economy continues to develop at comparatively high pace.

Table 4. GDP growth (corresponding period of the previous year = 100, %)

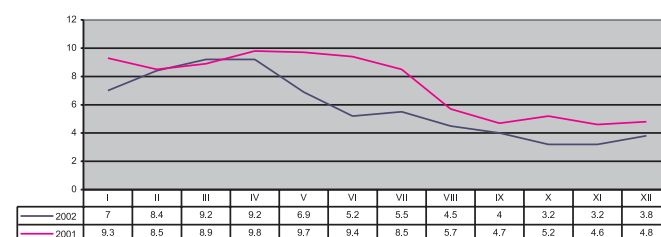
	Q3 2001	Q3 2002	Jan-Sept 2001	Jan-Sept 2002
GVA, total	4	4.5	3.7	4.6
GVA, agricultural sector	2.9	-0.5	0.4	0.1
GVA, industrial sector	5.7	4.8	5.4	4
GVA, service sector	3.5	6.3	3.6	6.1
GVA, private sector	7	6.8	6.8	7.9
GVA, public sector	-4.6	-2.8	-3.8	-3.7
Adjustments	3	5	6.5	2.5
GDP	3.9	4.5	4	4.4
Final consumption	2.9	2.5	3.9	2.5
Individual consumption	2.8	2.4	3.6	2.5
Collective consumption	3.4	3.8	5.9	2.2
Investments (GFCF)	15	6.3	15.8	7.4
Export (G&S)	13.6	5.9	12.5	1.3
Import (G&S)	22.9	-0.3	15.6	0.5

Source: NSI

Inflation

In the fourth quarter the monthly inflation rate is less than 1.2 per cent and is mainly a result of higher food prices compared to the previous month (October +1.8 per cent and December +2.8 per cent, with a share of 44.6 per cent in the cash expenditures of households), and in November - of higher service prices, particularly of housing goods and services³ (+1.1 per cent, with a share of 15.7 per cent in cash expenditures). But in the fourth quarter food prices are lower compared to the average prices for this group for the whole 2001. In the fourth quarter of 2002 the increase of consumer prices, taken on an annual basis, is more moderate compared to the increase in the corresponding months of 2001.

Figure 11. Inflation, corresponding month of the previous year = 100, %



Source: NSI

The National Statistics Institute plans⁴ to review in 2003 the big consumer basket of goods and services. Specification of the weights and names of some foodstuffs, a review of the method for calculation of electricity and heat prices imposed by the new step tariffs introduced in 2002 is at hand; prices of telephone services provided by BTC and the mobile operators will also be monitored.

According to the December business surveys conducted by NSI, increase of the selling prices in industry, construction, and trade is not envisaged. The possible war in Iraq will be a major pro-inflation factor in the months to come.

Labor Market

In the fourth quarter of 2002 the number of registered unemployed marked accelerated decrease (by about 20 thousand people in November and December compared to the previous month). The decrease of the number of unemployed is of a similar range along both channels of running unemployment survey: at the end of December the number of unemployed registered in the Employment Agency decreased by 42 thousand compared to September, and the number of

³ Housing (rent, routine repairs and maintenance), water, electricity, gas and other fuels

⁴ Announced at NSI's press conference on 13 January, 2003.

people who defined themselves as unemployed decreased by 40 thousand people according to the Labor Force Survey conducted by the National Statistical Institute.

The difference between the number of registered unemployed and the number of people who define themselves as unemployed is preserved - in December the number of registered unemployed increased by around 60 thousand people. Hidden employment has been partly confirmed by the first results of a large-scale joint examination conducted by the National Social Security Institute and the Employment Agency following the introduction of the requirement for mandatory registration of labor contracts with NSSI⁵. Results show that around 27 thousand people are registered both with the National Social Security Institute as employed and with the Employment Agency as unemployed.

NSI's business surveys of January 2003 do not indicate expected shrinking of labor demand in industry and retail trade; in construction expectations about the business and the employment in the sector for the next three months are strongly revised in a positive direction; a diffusion of opinions from optimistic towards moderate assessments and expectations about the business condition of enterprises, service demand, and labor force engagement is observed in the service sector (trade excluded).

Figure 12. Unemployed (thousands)



Source: EA, NSI

In the fourth quarter of 2002 the basic characteristics of the labor market improved compared to the corresponding period of the previous year. According to data from NSI's Labor Force Survey, in the fourth quarter of 2002 the seasonal decline of economic activity remains in the range characteristic for the previous year (around 140 thousand people), but there is structural improvement. In the period September - December 2001 the number of employed decreased (by 146 thousand people) and the number of unemployed increased (by 4 thousand people), whereas in the fourth quarter of 2002 both the number of employed and the number of unemployed decreased (by 99 thousand people and by 40 thousand people accordingly).

Table 5. Economic activity

		Sept.2001	Dec.2001	Nov.2002	Dec. 2002
Economically active people (labor force)	th.	3 407	3 265	3 388	3 249
- employed	th.	2 774	2 628	2 804	2 704
- unemployed	th.	632	636	585	
Economically inactive people (at the age of 15 and above)	th.	3 386	3 527	3 322	3 461
Economic activity coefficient	%	50.2	48.1	50.5	48.4
Employment coefficient	%	40.8	38.7	41.8	40.3
Unemployment coefficient	%	18.6	19.5	17.3	16.8
Manpower reserves ⁶	th.	419	514	436	509

Source: NSI

⁵ Communication by the press center of MLSP of 20 January 2003.

⁶ People at the age of 15 to 64, who are willing and ready to work, but are not active in seeking a job

Budget Implementation in the fourth quarter of 2002

Consolidated budget (includes the national budget and the judiciary branch budget)

According to the fourth quarter data generally the implementation of the consolidated fiscal program for 2002 was successful. The implementation of the revenues side corresponds to the adopted program. The revenues until December 2002 amounted to BGN 12,525 million, which is 100.9 per cent of the program. The expenditures amounted to BGN 12,743 million, which is 100.6 per cent of the program. There was a deficit of BGN 218 million.

Table 6. Implementation of the Consolidated Fiscal Program
As of the End of December 2002 (BGN million)

Indicators	2001 report	2002 program	2002 report	% implementation compared to the 2002 program
Revenues	11 838	12 406	12 525	100.9
Expenditures	12 093	12 663	12 743	100.6
Deficit	- 255	- 257	- 218	

Source: The Ministry of Finance

National budget (comprised of the central budget and budgets of government bodies)

At the end of the quarter it became clear that the annual implementation of the revenues side of the national budget was due mostly to the higher non-tax revenues, which compensated simultaneously the reduced taxes and social security contributions, and the higher (compared to the program) revenues from VAT resulting from the lower US dollar exchange rate. The overfulfillment of the revenues was BGN 307 million (BGN 6,982 million according to the program, compared to BGN 7,289.4 million as per the reports), which constitutes 104.4 percent, the tax revenues being 99.7 percent. The largest portion of tax revenues belongs to VAT - 36.9 per cent of the total revenues (however, it was planned to be 39.8 according to the program), and to the non-tax revenues - 25.2 per cent (while it was planned to be 21.9). The expenditures were BGN 7,600.7 million while the planned ones were BGN 7,528.1 million; that is 101 percent, which is a very good implementation of the expenditures side. The largest is the portion of capital expenditure - 53.8 of the total expenditure, social security funds - 40.3, and municipalities - 38.9. The national budget deficit was 0.6 per cent (compared to 0.5 per cent in 2001).

Municipal Finance

The overfulfillment of the revenues side of the budget by the end of the fourth quarter made it possible over BGN 621.8 million

to be granted for covering deficits under municipal budgets, for maintenance of schools, settlement of liabilities of hospitals, Christmas bonuses to pensioners and salaries in the budget-supported sector, and other priority expenditures. Throughout the year BGN 217.4 million were allocated additionally to municipalities, which - according to the Ministry of Finance - is the completion of the municipalities' obligation under the 2002 Program for Gradual Reduction and Complete Settlement of the Municipalities' Pending Costs, signed with the NAMRB.

The local finance reform is a lengthy and protracted process, the start of which was launched with the development and adoption by the Council of Ministers in July 2002 of the comprehensive financial decentralization concept. It covers the whole system of financial relations at all public governance levels.

Related to the foregoing were also the amendments to the Budget Act, the Local Taxes and Fees Act, the Corporate Income Tax Act, and others, which were adopted and entered into force on 1 January 2003. The most important of these are as follows:

2003 State Budget Act

Pursuant to Article 8 the revenues from taxes in compliance with the Natural Persons Income Taxation Act, with the exception of the one-time monetary compensations as per Article 237 of the Act on Defense and Armed Forces of the Republic of Bulgaria and Article 261 of the Act on Ministry of Interior, should be assigned 100 % to the municipal budgets.

Pursuant to Article 9 the fiscal relations between the central budget and the municipal budgets for 2003 are determined in the form of subsidies of BGN 385.9 million, and in terms of type they are: general complementary subsidies - BGN 270.9 million, general equalizing subsidies - BGN 15 million, and target subsidies for capital costs- BGN 100 million, per municipality.

The introduction of financial decentralization in municipalities has been adopted, starting on 1 January 2003, as follows:

- The local budget activities of a municipality will be funded with revenues from local taxes and fees, non-tax and other revenues;
- The funds from the ceded taxes as per Article 8 and the total complementary subsidies will ensure the full amount of the costs for salaries and social security payments, student grants and fifty per cent of the expenditures for upkeep, subsidies for health care and medical care, and for not-for-profit organizations, calculated according to the norms.

Provided that there is no violation of the budget deficit, the

Council of Ministers, following a proposal by the Minister of Finance, will cover with priority after 30 June 2003 the shortage of funds amounting up to BGN 130.1 million for supplementing the normal rate for current upkeep up to 100 per cent for mandated state activities to municipalities and within the relevant deadlines, and for Sofia municipality – up to BGN 25 million beyond the general regime. In case the foregoing cannot be applied, the Council of Ministers following a proposal by the Minister of Finance will organize consultations with the NAMRB for taking the required measures.

Expenditures for capital costs above the specified ones can be taken from municipal budgets, provided the source of funding are funds generated from local taxes and fees and other non-tax revenues, general complementary subsidies, as well as other funds stipulated by law. Funds from the ceded tax as per Article 8 and from the total complementary subsidies as per that Act cannot be used as source of funding for capital costs.

Corporate Income Taxation Act

A uniform rate of 23.5 per cent for corporate profits taxation is introduced pursuant to Article 44 of the Corporate Income Taxation Act, and the municipal tax is repealed.

Local Taxes and Fees Act

The Act on Amendments to the Local Taxes and Fees Act (LTFA) adopted at the end of 2002 effected a number of amendments to the regulation of local taxes and fees.

Some of the amendments have been in force since the beginning of the current year. The application of some of the adopted amendments has been scheduled for later times: 1 January 2004 and 1 January 2005. There is no change in the subject of taxation with local taxes: immovable property, heritage, donations, property acquired against payment, motor vehicles. Local fees as per the above mentioned Act will be paid for services and rights delivered by the municipal administration, such as: solid waste collection and disposal; usage of markets, market-places, pavements, squares, street lanes, fairs and areas with different purpose of use; usage of crèches, kindergartens, social care homes, camps and other municipal social facilities; recovery of quarry materials; technical services; administrative services; purchase of cemetery plots. From the items listed above it is obvious that there has not been any change in the range of services and rights, for the use of which local fees are payable. In case the municipality delivers other services and rights beyond the above-listed, then the Municipal Council will specify their prices.

Concerning the local fees the LTFA makes a substantial amendment to the previously existing procedure for setting their amount, as well as the exemption cases. The provisions applicable as of the end of 2002 regulated the services and

rights for the use of which local fees were to be paid, settled the cases of exemptions and reductions, the method of calculation of the fees and the admissible range of their amounts. The specific rates of the fees used to be determined by the Municipal Councils within the limits set by law.

Starting as of 1 January 2003 Municipal Councils are assigned the power to set themselves the size of fees for services and use of rights, as well as the order for complete or partial exemption from certain types of fees.

Each City Council has to adopt by the end of March 2003 its own Regulation on the setting and administration of local fees and prices of services.

Taxes and Duties

The implementation of tax revenues is BGN 5,436.7 million, while the program planned for BGN 5,450.5 million, that is 99.7 percent. The lower implementation of revenues from taxes as compared to 2001 (105.9 per cent of the amount in the program) is most probably due to the tax rates for corporate and individuals' taxes, which were reduced in the beginning of 2002. The highest implementation of revenues compared to that planned in the program came from customs duties – 188.4 percent, profit tax – 122.2 per cent and non-tax revenues – 120 per cent. The implementation of VAT was BGN 2,690.2 million, while the one planned in the program was BGN 2,779.8 million, that means 96.8 per cent implementation. The implementation of natural persons' income tax was BGN 531.7 million against BGN 557.4 million planned in the program, that is 95.4 per cent implementation.

In the fourth quarter a number of amendments to the taxation legislation were adopted and entered into force on 1 January 2003. Some of the main specific amendments to certain taxation acts (beside the ones described above) are as follows:

Corporate Income Tax Act (CITA)

The amendments to the CITA drew for the first time a parallel between the accounting and taxation legislation. The objective was to bring taxation concepts and terms in uniformity with the concepts and terms specified in the National Accounting Standards.

The annual depreciation rate for computers hardware and software is raised from 20 per cent to 50 percent. They are taken out of the group of assets with accelerated depreciation. The annual depreciation rate for assets of Group 2 – machinery, production equipment, motor cars and devices is increased from 20 per cent to 30 per cent with no permission for the accelerated depreciation method to be used. The annual depreciation rate of Group 3 assets – transport vehicles, road lining and aircraft runways – is raised from 5 per cent to 10 percent. The rule that

costs for assets repair should be adjusted for taxation purposes is repealed.

A tax relief is introduced for opening of new jobs in regions with high unemployment rate (50 per cent higher than the average in Bulgaria). A 100 per cent of the tax is ceded to producers who have made investment in such regions, under the following conditions:

- All sites and assets of the person to be located in that region;
- The number of opened new jobs to be increased by 10 per cent every next year;
- 80 per cent of the company's employees to have their permanent residence in that region.

Natural Persons Income Taxation Act (NPITA)

The non-taxable income is raised to BGN 1,320 per year and BGN 110 per month, respectively. The limit tax rates have been reduced (2-3 percent) for each of the brackets but the last one. The brackets hierarchy has been preserved, and the range of persons taxed with the highest limit tax amount (29 percent) includes all taxpayers with annual income over BGN 7,200, BGN 600 monthly income respectively. The monthly taxation scale for 2003 is as follows:

	BGN		BGN		BGN				BGN
non-taxable	up to 110								
From	110	to	150	tax	0	plus	15%	on the excess over	110
From	150	to	250	tax	6	plus	22%	on the excess over	150
From	250	to	600	tax	28	plus	26%	on the excess over	250
Over	600			tax	119	plus	29%	on the excess over	600

The proceeds from investments of assets of voluntary pension funds are exempt from taxation. The purpose is to achieve in the provisions of the NPITA uniformity in the taxation treatment of income obtained through voluntary pension insurance with similar income obtained on the basis of Life insurance, insofar as the latter was exempt from taxation pursuant to the NPITA starting from 1 January 2002.

The following have to be taxed with a final annual (patent) tax in 2003:

- Natural persons not registered under to the Commercial Code;
- Sole-traders;
- Local juridical persons;
- Local non-personified companies, which conduct the patent activities listed in Chapter 14 of the NPITA and their turnover for the preceding year is up to BGN 75,000.

If such persons carry out taxi transportation and transportation along additional bus routes, they are due to pay patent tax

regardless of their annual turnover for the previous year.

A significant characteristic feature of patent tax is that the law specifies it as a lump sum and the lump sum does not depend on the financial performance. Its amount is correlated with the functional type of the population center and the specific characteristics of the activities.

The requirement relating the patent taxation with an absence of registration under to the VAT Act is repealed. Starting 1 January 2003 only two criteria for taxation with a final annual (patent) tax will apply: annual turnover in the preceding year up to BGN 75,000 and conducting of activities as specified under Articles 31 and 32 of the NPITA. Annual turnover should be considered to be the net revenues stated in the profit and loss account for the preceding year. This means that the maximum possible turnover with VAT included, and within which the company meet the requirements for patent tax, is BGN 90,000.

In 2003 no patent tax will be due for performing the following activities: wholesale warehouses; construction and construction-repair services; hotels and other accommodation facilities with more than 20 rooms; catering and entertainment establishments with more than 100 seats; as well as retail trade on an outlet net area larger than 100 sq. m. The taxation for revenues generated through such activities in 2003 will be pursuant to the general procedure.

Excise Duty Act

Excise duty on wine is repealed. The excise duty on liquor is increased from BGN 0.035 to BGN 0.05 per volumetric percent. The excise duty on leaded petrol is increased as follows: with octane value less than 98 from BGN 300 per ton to BGN 400 per ton; with octane value 98 and higher – from BGN 550 per ton to BGN 650 per ton. The excise duty on unleaded petrol is increased as follows: with octane value less than 98 – from BGN 300 per ton to BGN 400 per ton; with octane value 98 and higher – from BGN 500 per ton to BGN 600 per ton.

Value Added Tax Act

The threshold for compulsory registration is reduced from BGN 75,000 to BGN 50,000. The change is welcome for small producers and traders, who will be able to receive tax credit refund. The purpose is to bring to the forth companies, which do not pay taxes and generate unfair competition.

With the permission of the Minister of Finance certain companies will be able to obtain an exemption from VAT for goods, which they import under investment projects amounting to over BGN 10 million, in the cases when the recipient of the consignment is a person registered pursuant to the VAT Act and the VAT amount is bigger than BGN 1,000.

Foreign and Domestic Debt

At the end of December 2002 the total amount of the government and government-guaranteed debt was BGN 18,180 million (recalculated as per the BNB central exchange rates of the Bulgarian Lev on 31 December 2002), which is 56 per cent of the Gross Domestic Product (according to the updated GDP estimate as per data from the Ministry of Finance). Compared to the end of the third quarter, there was a decrease of the total amount of the debt by BGN 748 million, which was due to an inconsiderable reduction of the portion of the debt denominated in US dollars, accompanied, however, by substantial reduction of the value of the US dollar exchange rate to the Euro as measured at the end of the two periods, respectively. The large drop of the ratio of the total debt amount as compared to (the estimate for) GDP, especially against the old data of the Ministry of Finance for the preceding months, is partially explained by the positive adjustment of the 2002 GDP estimate, which was made at the end of the year. According to the comparable data (the updated GDP estimate) the ratio debt/GDP decreased from 58.3 per cent at the end of September to 56 per cent at the end of December.

Expressed in US dollars, however, the total government and government-guaranteed debt increased by USD 102 million over the period from the end of September to the end of December 2002 (from USD 9,543 million to USD 9,645 million as per the BNB central exchange rate on the respective days). This is due to the increase of the Euro value to the dollar, accompanied by the change in the currency structure of the debt. The latter is explained not that much with the restructuring of the debt as of September, which was reported in the last quarter of 2002, but rather with the positive net internal financing. As of the end of September 2002 the debt denominated in US dollars was 51.60 per cent of the total amount of the government and government-guaranteed debt, while at the end of December the debt in US dollars was 49.79 percent. For comparison, the portion of the debt denominated in Euro increased from 27.20 per cent of the total amount as of the end of September to 28.35 per cent as of the end of December (the debt in Bulgarian Levs also marked an increase in the debt structure - from 7.32 per cent at the end of September to 8.21 per cent at the end of 2002).

In 2003 the amount of the debt will be predetermined once again by the dynamics of the Euro exchange rate to the US dollar and the change in the currency structure. In any case, however, the importance will lie with the ratio of the total amount of the debt to the GDP, which will probably maintain its improvement and will remain within the Maastricht criteria.

Foreign Debt

Bulgaria's active policy in foreign debt management in

2002 had its manifestation in the second (after the month of March) restructuring of our foreign debt in September. At that time Brady bonds were replaced by US dollar Eurobonds (through opening of the existing March issue of bonds with maturity in 2015). The summary results of the Ministry of Finance as of the end of the third quarter showed that Brady bonds amounting to a total of USD 866 million were exchanged against issued dollar bonds amounting to USD 759 million. The official data showed a net decrease of our foreign debt by USD 107 million, and release of the collateral to the value of applicable USD 135 million. Thus only from the operations in September the net decrease in the foreign debt according to the Ministry of Finance amounted to approximately USD 242 million. For the time-being this is the latest manifestation of Bulgaria's new active policy regarding the current management of the foreign debt.

The afore-described operation was reflected in the debt dynamics in the fourth quarter of 2002. For the period from the end of September to the end of December our foreign debt in Brady bonds (principal and accrued interest) decreased by the amount equal to the value of the bonds substituted in September. Due to the newly issued dollar Eurobonds and the increased value of the Euro, our foreign debt in Eurobonds increased by USD 815 million in the period under review.

As a result of the September restructuring operation, as well as due to currency rates fluctuations, in the period **from the end of September until the end of December the total amount of Bulgaria's foreign debt marked an increase by USD 12.6 million. Expressed in Bulgarian Levs, however, the increased value of the Euro resulted in foreign debt decrease by BGN 816 million over the above-mentioned period.** The total amount of Bulgaria's foreign debt, according to preliminary estimates as of the end of December 2002 was USD 8,524.6 million, which is BGN 16,069 million, recalculated based on the BNB central rate BGN/USD as of 31 December 2002 (of which amount: USD 7,978.4 million was government debt, and USD 546.2 million was government-guaranteed debt).

The data about the last month are preliminary ones. With a view to achieving comparability with past periods the above-used data regarding the amount of the foreign debt are based on information from the Ministry of Finance and do not include, for example, trade lending in the statistics of the gross foreign debt.

Beyond the repeatedly announced objective for improvement of the ratio foreign debt : GDP (due to the structure of the Bulgarian government debt this ratio is of crucial importance to the implementation of Maastricht Criteria), at present there **are still no indications of any existence or preparation of a long-term strategy for management of Bulgaria's foreign debt in particular.** However, the Government debt Act adopted

in the third quarter of 2002 can be assessed as a necessary step towards such a strategy.

The foreign debt dynamics statistics in 2002 do not confirm firmly the positive effects of the operations undertaken for restructuring the debt. Nevertheless, however, such restructuring and active management of the foreign debt received a completely positive assessment by investors. This was also one of the reasons for the further increase of Bulgaria's credit rating in the fourth quarter of 2002. In the beginning of October the biggest Japanese credit agency Japan Credit Rating Agency (JCRA) assigned to Bulgaria a "BB+" rating with a positive prospect of the long-term debt in foreign currency (this was the first credit rating assigned to Bulgaria by JCRA at all). Again in the beginning of October the international Rating Agency Standard and Poor's increased its rating for Bulgaria (the rating of the long-term government-guaranteed debt in foreign currency) from "BB-" with stable prospects to "BB" with positive prospect. At the end of October also the international agency Fitch IBCA raised (for the second time) the long-term credit rating in foreign currency - from "BB-" with stable prospects to "BB" with positive prospect. In mid-December 2002 Moody's international agency improved the prospect of that same rating of Bulgaria's (bonds and long-term securities) – from stable to positive, with the unchanged rating "B1".

Domestic Debt

As of the end of December according to data from the Ministry of Finance Bulgaria's domestic debt amounted totally to BGN 2,111.7 million (of which BGN 2,109.8 million government debt and BGN 1.9 million domestic government guarantees). Compared to the third quarter of 2002, there was an increase by BGN 82.1 million of the total domestic debt amount.

In the domestic debt structure as of the end of December the portion of the debt for government securities issued for financing the budget deficit was 69.24 % (while this percentage was 66.55 in the third quarter) of the total domestic debt amount. As of the end of December the portion of the debt for government securities issued for the structural reform was 30.67 per cent (while it was 33.3 per cent as of the end of September) of the total domestic debt amount. Again as a portion of the total amount, the domestic government guarantees comprise 0.09 per cent as of the end of December (compared to 0.15 per cent at the end of the third quarter of the year. Table 7 shows the dynamics of the structure of the total domestic debt amount.

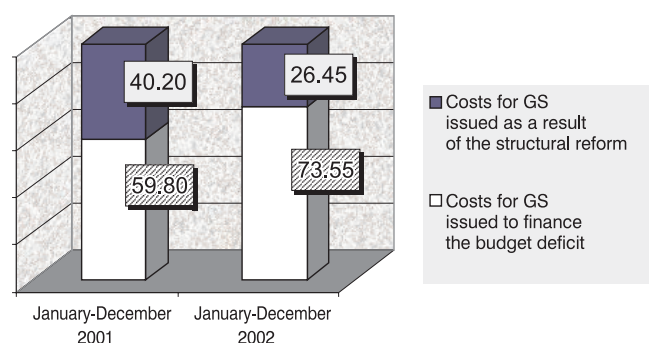
Table 7. Structure of the Total Domestic Debt Amount (%)

Debt structure	end of December 2001	end of September 2002	end of December 2002
Debt for government securities issued for financing the deficit	57.90	66.55	69.24
Debt for government securities issued for the structural reform	41.74	33.3	30.67
Domestic government guarantees	0.36	0.15	0.09

Sources: According to data from the Ministry of Finance, Government debt monthly newsletter

The total costs relating to the domestic debt (interests and discounts) for the whole year 2002 amounted to BGN 108.1 million (compared to BGN 126.8 million in 2001 excluding the costs regarding the direct debt to the BNB, which were reported until March 2001). In these costs the portion of the costs for government securities issued for financing the budget deficit was 73.55 per cent (compared to 59.80 per cent of the total costs for the domestic debt for 2001, but excluding the costs for the direct debt to the BNB), and the portion of the costs for the government securities issued for the structural reform was 26.45 per cent (compared to 40.2 per cent of the total domestic debt costs for the domestic debt for 2001, but excluding the costs for the direct debt to the BNB), Figure 13 illustrates the dynamics of the domestic debt cost structure for 2001 and 2002 respectively.

Figure 13. Domestic Debt Costs Structure (%)



Sources: According to data from the Ministry of Finance, Government debt monthly newsletters

In the months October-December 2002 the achieved primary market average yield from the newly issued government securities for financing the budget deficit was 3.58 per cent on an annual basis with the three-month bonds (three auctions in this period), 4.84 per cent on an annual basis with the 12-month treasury bonds (one auction in that period), 5.95 per cent with three-year treasury bonds (three auctions in that period), 6.70 per cent with the five-year bonds (two auctions in that period), and 7.40 per cent with seven-year bonds (two auctions in that period), according to BNB data (Government securities Market bulletin published by the Fiscal Services Division).

Thus regarding the domestic debt market the **fourth quarter marked a decreased yield from all newly issued government securities**, compared to the third quarter, and this decline was most strongly manifested **with shorter-term securities. Similarly to the preceding quarters the portion of securities issued for financing the budget deficit continued to increase at the expense of the portion of securities issued for the structural reform.** The portion of costs for government securities issued for financing the deficit also increased compared to 2001 as a direct result from the change in the domestic debt structure.

In the near future the government securities market will maintain the main trends of 2002. This refers to maintaining or decline of the yield from long-term issues in particular, increasing the portion of government securities and relative increase of the costs for government securities issued for financing the budget deficit, as well as gradual extension of the average maturity of issues in circulation calculated on the basis of the maturity structure of those bonds.

The domestic debt dynamics confirms that an active policy for its management is in place, similarly to the new policy for the foreign debt, which has been in place since the autumn of 2001. However, in this case again, it is not quite clear to what extent this policy is a part of a long-term strategy for the debt management. Prevalent is the expectation that the government securities market will be a main priority for the Ministry of Finance in 2003, where the domestic debt portion of the government debt and government-guaranteed debt as a whole will be increasing. The two most important limiting factors for the development and management of the foreign and domestic debt will be the observance of the Maastricht criteria and the application of the **Government Debt Act** adopted in September 2002.

In the fourth quarter of 2002 the pace of privatization in the government sector remains unsatisfactory in terms of both proceeds and concluded transactions. Only 16 companies where the State holds a majority interest and 12 detached parts were sold. Government's intentions to accelerate the privatization process, to animate the capital market offering for sale shares of big and attractive companies, and liquidate the minority interest of the State in more than 1 350 companies were not fulfilled.

With a 2002 annual plan of 664 privatization transactions, including sale of 238 companies where the State holds a majority interest⁷, till 31 December 2002 the number of privatization transactions concluded was only 275, according to data by PA⁸. The annual plan is fulfilled at 41.4 per cent. The number of enterprises with majority interest sold is 73. The annual plan for these companies is fulfilled at 31 per cent.

Government's expectations to finalize the two biggest privatization transactions - for BTC EAD and Bulgartabac - Holding AD, did not come true. The preparation of these transactions was delayed in the very beginning because the new PPCA was passed behind schedule and the Parliament approved with delay the privatization strategies of these companies. The procedure for Bulgartabac - Holding was opened on 25 March, and that for BTC EAD - on 2 April, 2002. The two procedures were accompanied by repeated extension of time limits, which generated a negative social effect and suspicions about legal violations.

The actions of the Privatization Agency in the sale of **Bulgartabac Holding AD** can serve as an example of unnecessary prolongation and complication of procedure. On 22 July, 2002 Tobacco Holding, Rosbulgartabac and Metatabac Consortium filed their final offers. The latter were valid for 120 days. The Agency requested additional explanations to the offers. Having received the replies, the Agency disqualified Metatabac Consortium on account of incompleteness. Then PA took time to prepare a report on the progress of the privatization procedure. The report was submitted to the Council of Ministers for discussion. CoM's decision was in the form of instruction - PA should determine the exclusive buyer without further requests to improve offers. Conforming to this decision, the Privatization Agency appointed the Tobacco Capital Partners-Clar Inis B.V. Consortium exclusive buyer of 80 per cent of Bulgartabac Holding. Objections by the opposition, the trade unions, and independent experts concerned the extremely unfavorable selling price of the company and the considerable reduction of the number of jobs. PA's decisions were later attacked in court, which further prolonged and complicated the process.

In October 2002 the Supreme Administrative Court proceeded with the case of the privatization transaction for Bulgartabac Holding, admitting for consideration the appeals of the three dropped out candidate buyers. At the end of the same month a three-member bench of the Supreme Administrative Court reversed the decision of PA's Executive Director (No. 2101-П/23 August 2002) whereby the Tobacco Capital Partners-Clar Inis B.V. Consortium was declared exclusive buyer of 80 per cent of the capital of Bulgartabac Holding.

The lack of precision in PA's and Government's actions prejudiced the fulfillment of Bulgaria's obligations towards the World Bank, the tobacco buy out price, the operation of Bulgartabac Holding. According to politicians and experts, the public dispute between the Government and the court had a negative effect on country's investment climate.

The decision of the three-member bench of SAC was appealed before a five-member bench of the court. On 16 December 2002, a five-member bench of SAC confirmed the force of the decision whereby Bulgartabac Holding's exclusive buyer appointed by PA was recalled. The court referred the matter back to PA with an instruction to continue the procedure by requesting candidate buyers to improve their offers. According to the court, by failing to honor the requests for price improvement of the three potential buyers who remained out of the classification, PA violated the regulation on competitions as well as the privatization strategy of the company.

The appointment of buyer of **BTC EAD** also aroused the interest of the society. Politicians, trade unions, and experts took different views. On the one hand, the appointed buyer was approved (the company Viva Ventures registered in Vienna and owned by the US investment fund Advent), on the other hand the parameters of the offer filed - price and number of jobs preserved, were subjected to criticism.

PA's appointment of buyer was attacked in court by the non-government organization Internet Society, by UDF, CITUB, and by the Supreme Prosecutor's Office. As a result of the appeals PA suspended negotiations with the appointed buyer until the case was determined.

Thus at the end of 2002 the privatization of these two companies was not completed yet. That influenced the overall execution of the revenue part of the Annual privatization plan.

An alarming trend observed as early as the third quarter of 2002 is also worth noting - all parliamentary groups introduce to the National Assembly **various proposals for amendments to the newly passed PPCA**. Five bills for amendments to PPCA were introduced only in the period from 24 September till the end of 2002. It should be reminded that a major criticism towards the repealed Privatization Act (by members of this Government as well) concerned the numerous (over 30) amendments in the

⁷ 2002 Operation Plan of the Privatization Agency, www.priv.government.bg

⁸ Report by Apostol Apostolov - Executive Director of PA, www.priv.government.bg

ten years of its effectiveness, which considerably altered and impeded its application in practice.

A careful insight in the new proposals reveals that these are directed towards protecting the interests of individual departments or economic groups, contrary to the clearly formulated objective of the new act: fast, transparent and economically efficient privatization.

The bill introduced in December (and subsequently withdrawn) by MP Miroslav Sevlievski and a group of MPs from National Movement Simeon II is among the most contradictory proposals. The essence of the requested amendment to PPCA is in closing down the Privatization Agency and setting up a fundamentally new structure to carry out the privatization process - Bulgarian Privatization Holding EAD. According to the bill, this privatization holding will be set up as a joint-stock company with state interest. The provisions of Art. Art. 277 through 280 of CC will apply to it. The state interest in all commercial companies intended for privatization will be deemed transferred to the holding. The minister of the economy will exercise the rights of the State as a sole proprietor in this holding.

After long drawn out lawsuits, reversal of PA's decisions by the court, and numerous appeals disputing the selling procedures of BTC and Bulgartabac Holding, the ruling majority obviously wants to legally avoid the control by the independent judiciary on the work of the Government and PA. Comments on the amendments to PPCA adopted in the beginning of 2003 were quite similar.

Several events in the sector of small and medium-sized enterprises are worth noting for the last quarter of 2002. Most of them are directed at improving the conditions of the business environment, which have significant effect on the development of Bulgaria's small and medium-sized businesses.

In the beginning of October the Vice-Premier and Minister of Economy introduced in the National Assembly a **package of measures to improve the business environment and promote the economy till mid 2003**. The project aims at increasing employment, improving social security, and achieving higher standards of living for Bulgarians. The package of measures envisaged to enhance the role of the Bulgarian Export Insurance Agency (BEIA) by way of increasing its capital from BGN 10 million to BGN 30 million with a view to expand its capacity. A tax reform project envisaged introduction of zero rate profit tax in regions with high levels of unemployment, reducing the minimum thresholds of voluntary and mandatory VAT registration to BGN 50 thousand and BGN 25 thousand accordingly, and preserving the 7 per cent VAT rate in tourism. Amendments to the Commercial Code were also introduced in Parliament. Their aim is to accelerate and radically simplify insolvency and bankruptcy procedures, with a view to enable finalization of the whole procedure within a couple of months. (For more information on the package of measures see the section Other Elements of Business Environment).

The proposed package of measures to improve the business environment was subject of extensive public discussion. One of the adopted measures included **lowering the minimum threshold of VAT registration to BGN 50 thousand, which would enable small and medium-sized businesses to get tax credit in 2003**. Thereby the preferential treatment of the big business is partially eliminated and an opportunity for registration of some small and medium sized companies under VATA is provided.

Access to financing remains a serious barrier to the development of Bulgarian small and medium-sized companies. A positive sign in this field is the more intensive competition of commercial banks which penetrate the sector of lending to Bulgarian small and medium-sized businesses. The schemes of Government support to SMEs, including Government guarantees for bank loans, are still in their initial stage and the number of beneficiaries remains limited yet. **Since October 2002 the Encouraging Bank AD started in cooperation with the Agency for Small and Medium-sized Enterprises a running competition for new projects.** All companies that have taken a loan from the bank within the corresponding quarter may take part in one of the four programs:

- Investment lending to small and medium-sized enterprises;
- Long-term investment lending;
- Investment lending under SAPARD
- Improving the competitiveness of Bulgarian products.

The winner in the competition will be charged an interest on

the provided loan, which is by two percentage points lower than the average interest rate on long-term corporate loans in the country. This new competition in the SME field aims at encouraging young entrepreneurs to generate innovative business ideas and at supporting promising business undertakings.

At the end of October Encouraging Bank received a credit line of EUR 15 million from the Development Bank with the Council of Europe. The funds are allocated to finance investment projects of Bulgarian small and medium-sized companies with a view to create new jobs and preserve existing ones. The loan has a 10 year redemption period and funds will be utilized in four trenches for a period of 2 years. EUR 10 million are secured with a Government guarantee. Most funds will be used to provide long-term (4 to 10 year) investment loans to small and medium-sized enterprises, with a grace period of 3 years. The other portion will be used to finance 1 to 4 year investment loans. Despite this new credit line (which completes the list of similar lines for Bulgarian small and medium-sized companies available for several years already), a conclusion can be made that Bulgarian commercial banks are still unwilling to provide loans for development of Bulgarian small and medium-sized businesses on account of the persisting problems with the securing of guarantees.

Since 2003 e-Government and the "one-stop shop" administrative service are expected to facilitate citizens and the business in making use of Government administration services. The e-Government strategy was developed by a working group of Government administration representatives in cooperation with non-government organizations. (For more information on the subject see section Other Elements of Business Environment).

The 2002 Regular Report of the European Commission on the progress of Bulgaria was published in October. It states that "Bulgarian policy for small and medium-sized enterprises largely conforms with the principles and goals of EU's policy in respect of enterprises, but the lack of resources and coordination, as well as the ambiguous perspectives of the institutional organization in the SME field, have limited the efficient implementation of the policy for SMEs". Further efforts to improve the awareness of enterprises about the changes undertaken by the Government in the field of commercial and tax legislation are recommended. It is important to define mechanisms to assess the barriers to the development of Bulgarian small and medium-sized businesses, as well as to secure the future of Government organizations supporting SME development, and to improve their operation with a view to successful EU integration of the Bulgarian SME sector. The problem with the absence of powerful business organizations representing the interests of small and medium-sized enterprises is not solved yet. The question of the **definition of SMEs applied in Bulgaria, which is not brought in conformity with EC recommendations yet** remains unregulated.

Foreign Economic Relations

Low growth of world economy and insufficient demand on international markets did not impede **the increase of exports that started as early as the second quarter, compared to the end of 2001. According to preliminary data exports of goods during the fourth quarter amount to USD 1 414.1 m. According to our assessment after the subsequent revision this indicator will reach at least USD 1 500 m, which would mean about 18 per cent more than the same period of 2001.** In comparison to the third quarter a certain decline is observed, but historically this is the most intensive period of the year in terms of exports.

Most significant growth in the fourth quarter of 2002 compared to the same period of 2001 was reached in the exports to CEFTA countries – almost 30 per cent. Thus their share in the total Bulgarian exports reaches 6.3 per cent (with 5.4 per cent a year ago). Exports have significantly grown also in the trade with EU countries – around 18 per cent, thus their share reaches 55.6 per cent. Changes in the positions of some other major trading partners of Bulgaria are insignificant. Exports to Turkey grow by 14 per cent, thus keeping its share of about 9 per cent, while the relatively low growth (about 6 per cent) of exports to the Balkan countries (mainly Yugoslavia and Macedonia) leaves them with a share of 6 per cent (with 7.6 per cent a year ago). It is only the exports to CIS and Baltic countries that decrease by 17.5 per cent, most serious being export shrinkage to Russia (by 25 per cent).

From the view point of commodities structure exports of products from almost all groups (except for energy resources) is growing at accelerated pace. Highest growth compared to the fourth quarter of 2001 is observed in the exports of investment goods (mainly machinery and equipment) – 29.3 per cent. The growth of 17.8 per cent in the exports of raw materials and inputs is due to the high growth (32 per cent) of exported ferrous and non-ferrous metals. The stable positions of Bulgarian textile products on the international market, the 50 per cent growth of exports of furniture and household equipment and almost 30 per cent of foods lead to an increase of over 15 per cent of the total value of consumer goods exports. As a result, the shares of different commodity groups in the total exports have changed: investment goods now account for 14.7 per cent (with 12.7 per cent in the fourth quarter of 2001), raw materials – 42.4 per cent (40 per cent in the same period of last year), consumer goods – 36.3 per cent (35 per cent in the same period of last year). It is only with energy resources that decline of exports is observed both in terms of total value (by 40 per cent) and their relative share (from 12.2 per cent to 6.6 per cent).

According to preliminary data in the last quarter of 2002 imports (CIF) have increased by about 20 per cent compared to the same period of 2001 and amount

to USD 2 339.8 m. In our opinion, however, these data are also subject to revision and probably imports increase will be at least 24 per cent. It is possible that the high growth of imports in the fourth quarter is related to the desire to ensure raw materials for the production in case of deterioration of the market with regard to possible war operations against Iraq. In support to this statement is the fact that highest (by 22 per cent) is the growth of exports of raw materials and inputs, and lowest (15 per cent) – that of consumer goods. Nevertheless, the share of individual commodity groups in the total import remains almost unchanged – 26 per cent, energy resources – 20 per cent, raw materials and inputs – 34 per cent, consumer goods – 20 per cent. This allocation makes it clear that 80 per cent of imports are designed for production use (mostly for production of goods designated for export).

According to preliminary data the trade balance deficit (exports FOB – imports CIF) amounts to USD 925.7 m or by around 40 per cent more than in the last quarter of 2001. Following data revision this deficit will probably prove to be smaller but the difference will not be significant. In any case, deficit in exchange of goods in the fourth quarter will present around 40 per cent of the total one for the year. Deficit increase compared to the one for the same period of last year is off-set by its decrease over the previous two quarters and its annual amount will not exceed that of 2001.

Measures were undertaken to improve Bulgarian manufacturers' access to foreign markets. A Free Trade Agreement was signed in October with Latvia. Implementation of the agreement is expected to result in improved trade and economic relations between the two countries. Negotiations were finalized for free trade agreements with Albania and Yugoslavia. Yugoslavia ranks third among the Balkan countries in commodities exchange with Bulgaria, following Greece and Turkey. During the first years of implementation of the agreement the commodities exchange between Bulgaria and Yugoslavia is expected to increase by 20-25 per cent. An agreement was signed in October for liberalization of trade in fish and fish products between Bulgaria and EU. The agreement is in the form of an Additional Protocol to the European Association Agreement. This document envisages liberation of trade in fish and fish products, divided in two lists.

Foreign Investments

The picture of foreign investments inflow corresponds to the current situation on international financial markets characterized by general uncertainty and suspension of investment projects due to the expected war in Iraq and low pace of growth of the world economy. Neither foreign, nor domestic conditions (lack of favorable incentives) are conducive to making a decision on a green-field investment in Bulgaria. Due to the scandals around the Privatization and Post-Privatization Control even planned large privatization transactions were not realized.

Preliminary data on the volume of foreign direct investments that entered Bulgaria in the fourth quarter of 2002 mark a considerable increase compared to the third quarter and a slight drop down compared to the fourth quarter of 2001. The picture looks quite different than a month earlier due to the serious revision of data from BNB. The total level of investments for the last three months of 2002 is estimated at USD 203.2 m and accounts for 44 per cent of the annual level (USD 458 m). Proceeds from privatization for this period (USD 72.9 m) are by 14 per cent more than in the first three quarters taken together. Proceeds from other (non-privatization) transactions amount to USD 87.1 m and exceed the levels recorded in the previous three quarters. However, compared to the fourth quarter of 2001, these are reduced by one half. Overall, equity investments (from privatization and other transactions) are almost equal to those from the previous year.

Most intensive dynamics during individual months is observed in the change of net payables between companies with foreign interests and direct foreign investors under various inter-company loans. Therefore, these data are subject to most serious revision. The inflow of borrowed funds under this item for the last three months of 2002 amounts to USD 43.3 m, which seems to give some hopes for reversal of the trend of negligible low or even negative net amount of inter-company loans in the second and third quarter of 2002. A cause of concern is the zero amount of reinvested profit though data might be revised later on.

By all means it seems that in close future again cash inflows from parent companies to their joint ventures will remain the most important source of foreign direct investments, because neither the declared acceleration of privatization, nor the desired attraction of green-field investments will be possible.

Government Policy

The political debate about the future of the Kozloduy Nuclear Power Plant (NPP) in connection with the Bulgaria's position in the negotiations with the European Union on Chapter 14: Energy dominated the government policy in the energy sector. Chapter 14: Energy of the negotiations for Bulgaria's accession was closed in the middle of October. That was made possible after the Bulgarian Government submitted additional information where 2006 was stated as closing year for units 3 and 4 of the Kozloduy NPP.

In the course of the negotiations the Government reached an agreement for a peer review of units 3 and 4 to be carried out by the European Commission in 2003. The Government plans to continue the negotiations after the inspection and has stated that it will accept a Commission's position based on expert evaluation of the reactors' conditions.

In its position on Chapter 14: Energy the Government did not conform to Bulgarian Parliament's decision, which was taken with great majority achieved with the participation of all political forces represented in Parliament, that the reactors should not be closed before the date on which Bulgaria would become an EU member,. That gave grounds to a group of MPs to attack in the court the Government's decision for the decommissioning of the small units. In the beginning of 2003 the Supreme Administrative Court (SAC) reversed in part the Government's decision. The part concerning the complete and final closure of units 3 and 4 of the Kozloduy NPP was declared illegal because "the comprehensive analysis of the possibility to maintain and increase the level of safety and management of the nuclear facilities resource in conformity with the national legislation and the obligations resulting from the Convention for Nuclear Safety"⁹ had not been presented. According to the Energy Strategy of Bulgaria it is this analysis that the decision to close units 3 and 4 should be based on. The SAC's decision was appealed by the ministers of energy, foreign affairs, and European affairs.

At the end of the quarter under review **Bulgaria closed units 1 and 2 of the Kozloduy NPP** in accordance with the 1999 arrangements with the European Union. Thereby the electricity production capacity of the country was reduced by 880 MW to around 12 GW. The early decommissioning of the oldest units in the nuclear power plant will not threaten the stability of national electricity supplies in the short-term because spare production capacities are available. It could result in a slight increase of the average electricity prices on a national scale because the Kozloduy NPP is the producer selling electricity to NEK at the lowest price. However, two factors will restrict the price increase. First, the nuclear power plant sells its availability (which is paid separate from the electricity produced) at one of the highest prices among all independent producers. Consequently, after the closure of units 1 and 2 the average

system availability price drops down. Second, the more intensive use of other power plants will result in distribution of their fixed costs over a greater amount of electricity sold, which will finally lead to reduction of their selling prices.

Table 8. Electricity selling prices of independent producers (VAT excluded)

Independent producer	Electricity price (BGN/MWH)	Availability price (BGN/MWH)
Kozloduy NPP EAD	18.93	18.90
Bobov Dol TPP	44.10	11.37
Maritza 3 TPP EAD	41.69	20.32
Toplofikatzia Russe EAD (unit 4)	37.17	7.90
Varna TPP EAD	39.12	4.07
Martiza-Iztok 2 TPP EAD	26.60	14.05

Source: State Energy Regulatory Commission
http://www.dker.bg/bg/documents/dker_docs/prices_all.pdf

For the time being the decommissioning of the two nuclear units do not have any effect on the unemployment level in the region of the town of Kozloduy. The teams that operate the units continue to work because maintenance is required even after the closure. The Nuclear Regulatory Agency is expected to issue in the first quarter of 2003 a license for long-term operation of the two units excluding the right to produce electricity, with a view to guarantee safe fuel storage.

In November the Ministry of Energy and Energy Resources proposed a **new energy legislation concept paper**¹⁰. The intentions stated give some idea of the framework within which the sector will develop in the years to come. It should be noted, however, that some parts of the concept paper, particularly those on the heating and natural gas sectors, state the issues to be regulated by the law but do not sufficiently specify the essence of these fields. All that predetermined the process of further clarification of proposed ideas and texts, which continues even in the first quarter of 2003.

According to the concept, two acts will form the backbone of the regulatory framework in the sector. The Energy Act will regulate the relations concerning the production, transimission, distribution of and the domestic and foreign trade in natural gas, electricity and heat. The Energy Efficiency Act will build the regulatory environment for rational use of energy, for reducing the harmful impact on environment, and for expanding efficient energy services for the society.

The Energy Act concept envisages a wider introduction of market relations in all activities, from the production to the end-user supply of electricity, heating and natural gas. A positive fact is that the all market actors are covered and all possible

⁹ Energy Strategy of Bulgaria, Sofia, 2002, www.doe.bg

¹⁰ The full text of the new energy legislation concept paper is available on the Internet site of the Ministry of Energy and Energy Resources www.doe.bg

relationships among them are identified. The concept introduces the idea of trade with energy as a separate activity from the operation of the infrastructure enabling supplies between the separate units along the value added chain. The separation of the group of traders paves the way for competition in the sector, because traders do not need infrastructure but only to sign contracts with the operators of production, transmission, and distribution facilities.

The envisaged elimination of permits for construction of energy facilities and their integration in licenses for use of these facilities also has a favorable effect on the business environment in the sector because administrative barriers are thereby reduced. Raising twice the upper limit for the capacity of electricity production facilities, for the construction and utilization of which permits and licenses shall not be required, will encourage entrepreneurs, particularly in the construction of small plants operating on water, solar energy and other renewable energy sources.

The competences of the Ministry of Energy and Energy Resources are limited to implementing the Government energy policy, supervising the balance of demand and supply, and initiating construction of new electricity production and gas distribution capacities, provided that there is a demand for such capacities but no initiative comes from the business circles. At the same time, the role of the State Energy Regulatory Commission is enhanced. It should undertake all functions related to licensing, price regulation, formulation of business rules, control on the observation of introduced requirements, and sanctioning. The concept confirms the idea of clear differentiation and division of functions between the two state institutions.

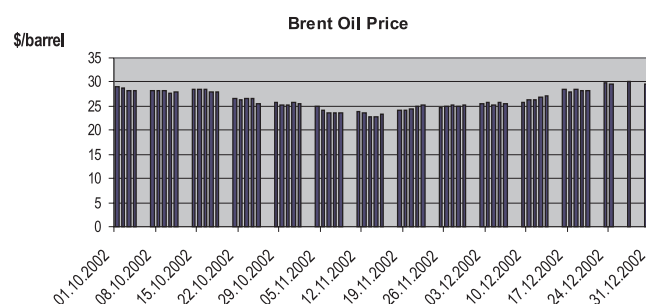
Establishing energy efficiency as a Government policy priority is the idea underlying the **Energy Efficiency Act concept**. The Energy Efficiency Executive Agency will continue to head the administrative policy in this field. The concept also presents the basic tools to be employed to encourage energy efficiency. These include mandatory energy assessments of investment projects generating large energy consumption, and encouraging the set-up of special enterprises for energy efficient services. Establishment of a fund to provide low-interest loans for energy efficient projects is another measure set forth in the concept. The envisaged accumulation of assets for the fund by way of an extra charge on the price of conventional fuels will result in higher costs for all energy traders, which will ultimately be transferred to end-users.

With a view to encourage implementation of energy efficient measures, the concept sets forth the idea of tax reliefs, without mentioning any particular figures.

Energy Prices

In the fourth quarter of 2002 crude oil quotations at international markets remained at high levels, moving upwards to the level of USD 30 per barrel since mid December. Their dynamics was dictated in the first place by the situation around Iraq and the problems possible military operations would create for the normal oil supplies from Middle East countries.

Figure 14. Crude Oil Price Dynamics



Source: International Oil Exchange, www.ipe.uk.com

Given the high share of crude oil import in national consumption, international market dynamics was reflected in Bulgaria as well. Fuel prices on the domestic market increased. The effect of the higher oil products price levels was mitigated by the downward trend in the dollar exchange rate at the end of 2002. Higher fuel prices affected mostly the transport sector, and due to the stabilization of fuel prices at higher levels transport operators began to raise the prices of their services, thereby transferring the additional costs to their clients.

Quotations at international markets also influence national supplies of natural gas, but the State Energy Regulatory Commission did not change the price at which Bulgargas sells natural gas on the domestic market. Two factors justify such a decision. First, Bulgargas pays crude oil supplies in US Dollars and the lower quotations of the currency partially neutralize the higher price levels of crude oil. Second, in previous months supplies were made at lower prices, hence the price at the domestic market lags behind with a smoother variation international oil exchange dynamics.

Pegged natural gas prices are good news for Bulgarian industry, because its raw material costs will not increase. This is beneficial for district heating companies and for public and industrial power plants, which account for around 37 per cent of the national natural gas consumption.

The changes in the Bulgarian aviation business dominated the government policy related to the transport sector during the last quarter of 2002. The main objective of those changes was to preserve the state role in the civil aviation.

Those changes were predetermined by the decision of the general assembly of the creditors of Balkan Airlines to reject the rehabilitation plan offered by the trustees in bankruptcy. Thus conditions were created for implementing the idea of establishing a new company to carry the national flag. Balkan Air Tour, which operated as a ticket sale agent at the Sofia Airport by then was declared such a company. Within a comparatively short time period the Ministry of Transport and Communications in its capacity of an owner of the new company managed to initiate its flights and authorized it to carry the national flag under the international agreements with several countries including Germany, United Kingdom, France and Russia.

Declaring Balkan Airlines insolvent led to temporary difficulties in servicing its clients. The new national carrier undertook to fly those passengers which brought it an initial loss of about BGN 2.3 million.

The liquidation of a national carrier and its replacement by another company is not something new in the European aviation. During the last two years Swiss Air and the Belgian Sabena became illustrative examples of such transformation. However, there are three significant differences between those two cases and the situation in Bulgaria, that may become crucial for the market viability of the new national carriers.

Firstly, in Switzerland and Belgium the national carrier has been succeeded by its daughter company, operating at that time as a regional carrier. In addition to its experience and reputation as aviation operators, the new carriers of the national flag - Crossair (renamed later to Swiss) and DAT could rely also on part of Swiss Air and Sabena assets that were transferred to them before the liquidation of the two companies. In Bulgaria the new national carrier does not have an immediate experience in air transport and will rely on the human resources of Balkan Airlines to compensate for this disadvantage. Balkan Airlines bankruptcy estate will be cashed and cannot be transferred to Balkan Air Tour as the last one is not its legal successor. Consequently, the new carrier has to provide equipment for the new activity which means large expenses irrespective of the present favorable aircraft leasing market.

Secondly, the private business in Switzerland and Belgium supported the revival of the national operators. Even more: in Crossair case the private business not only secured the funding but also initiated the establishment of a new national carrier. The private sector in Bulgaria stayed aside from those efforts. The financial injection for the start of the new carrier has

been received in full from the state which is a sole proprietor of the company. Despite the intentions for quick privatization of a less than 50 per cent share of company equity and even for parallel privatization with constituting the company as a national carrier, the participation of the private sector remains only a good wish.

Last but not least, the huge difference in the funds that had been secured for starting the activities of the new carriers should be mentioned. In Switzerland the private sector, natural persons, central and local governments provided jointly more than EUR 2 billion to Crossair. In Belgium 12 Belgian banks and 3 regional investment companies raised EUR 200 million, and in Bulgaria additional funding of about EUR 15.3 million has been secured.

Under the conditions of a very competitive and stagnating aviation services market, the question arises whether and how Balkan Air Tour would manage to secure its sustainable competitiveness. Because of the problems of its predecessor that continued for several years, the foreign airlines managed to penetrate the niche of the air transport from and to Bulgaria. Favorable data about tourism in the country and the expectations that the number of foreign tourists will increase during the next years holds out good opportunities for the new carrier. The ability of the company to use those opportunities for its own benefit depends on the quality of the product that it will offer. The bad positioning on the market may transform Balkan Air Tour into a loss generator, and the losses would have to be covered by the state.

The state-owned companies in the railway transport continued to experience financial difficulties. The increasing losses of the companies that reached BGN 6 million for the infrastructure company and BGN 31¹¹ million for the carrier during the first half-year, necessitated granting of BGN 12 million temporary financial aid to the Bulgarian Railways. Despite the statutory regulations allowing private companies to enter the sector, the Bulgarian Railways are still a monopolist. If part of its profitable destinations experience serious competition by the private sector, the financial difficulties of the company will intensify. The financial problems of the state carrier cause social tensions and a risk of strikes and eventually that has a negative impact on the quality of the railway transport.

The Regular Report of the European Commission on the progress of Bulgaria was released in the beginning of the quarter. The Transport Policy Chapter has not been closed yet and the negotiations on that Chapter emerge as difficult ones because of **the poor technical condition of the vessels under Bulgarian flag**. Those negative impressions reflect not only on the negotiation process, but on the maritime business,

¹¹ The data are from the Ministry of Transport and Communications, <http://www.mtc.government.bg/Presscenter/News/October/oct-24.htm>

too, as the clients' confidence in carriers decreases. The adoption of new legislation related to maritime safety and its strict enforcement represents an opportunity for overcoming the negative impacts.

The negotiations with the contractors selected for executing **construction works on the transport infrastructure** have been completed during the fourth quarter. Those works will help for improving the business environment in the country. They include the construction on a new passenger terminal and a new runway at Sofia Airport and two new sections of Trakia highway.

The results from the last quarter did not change significantly the total rating of the state and development of high technology in the country during the last year. The situation in the sector did not go through any serious transformations and problems, except for may be the tension about BTC JSC privatization and the lack of clarity regarding the new Telecommunications Act which had not been put forward to the vote in the Parliament till the last days of the year.

At the end of the year (on 19 December), after a long delay, the **Council of Ministers adopted a Strategy for Introduction of e-Government in Bulgaria**. As it was already commented upon in the previous releases of the quarterly review of Bulgarian economy, the Strategy represents a landmark document for the creation of e-Government and an action plan will be drafted subsequently on its grounds. The adoption of the Strategy proves the commitment of the Government to accomplish the undertaken tasks for up-dating and refinement of state administrative procedures and improvement of services provided to the citizens and companies in the country. In the 2003 state budget, however, there are no provisions for e-administration funding and in this case the government will obviously rely again mostly on the support of different donor programs in that area.

Together with the Strategy, the Council of Ministers passed also a resolution for **participation of Bulgaria in IDA II Program of the European Union** - data exchange among the administrations during 2003-2004 period. IDA Program is European Union tool aimed at establishing a uniform information space for data exchange among the administrations of the European Union member and candidate countries with the appropriate security of information exchange. The uniform information space will be created through formulation, development and use of uniform technical and software solutions. The mission of IDA Program is to support the implementation of European Union policies and activities by coordinating the building up of trans-European telecommunication networks among the administrations.

At the end of 2002 (on 27 December) **the amended Corporate Income Taxation Act was promulgated**. The Act came into effect on 1 January 2003. According to the new law the annual depreciation of computers, software and software licenses is 50% which means that for tax purposes the computer equipment and software could be depreciated in 2 years. This amendment has a huge importance for the development of the information and communication technology (ICT) business and its adoption is a big step in the right direction. It is a different issue that such an idea has been discussed among the business for more than two years and that amendment comes late.

On 19 November 2002 **the European Bank for Reconstruction and Development approved a project for funding the second Bulgarian GSM operator GloBul**. The funding amounts to EUR 90 million, EUR 80 million being a

credit and the other EUR 10 million being equity interest in the telecommunication company. The funds are intended for purchase of equipment and services for the future development of GloBul network.

At the end of October the Ministry of Economy presented a **draft of an Innovation Strategy for Bulgaria and Measures for its Implementation**. The main objectives of the strategy are: increasing the competitiveness of Bulgarian industry, strengthening the scientific and technological sector and creating favorable conditions for young specialists in the field of research and technology.

Four steps are necessary for the achievement of those objectives according to the Strategy:

- Development of the so-called National Innovation System which will cover all institutions, companies and organizations working in the development, exchange and know-how implementation field;
- Ensuring the cooperation between the research and technical sector and the business;
- Establishing national organization for coordinating the adoption and implementation of the Strategy in the innovation field. It includes National Innovations Council composed of representatives of the line ministries, contractors, researchers/technologists, as well as executive body responsible for the implementation of the Strategy;
- Securing adequate funding for implementation of the measures included in the Strategy.

Thirteen specific measures have been proposed in the draft document. They include: stimulating prospective research and market oriented technology projects; encouraging the employment of young specialists in the field of research and technology in SMEs; establishing incentives for attracting foreign investments in the research and science fields and crediting the development of new products in small companies.

Some **preliminary data about the ICT market volume in Bulgaria in 2002** have been presented in the fourth quarter of last year. IDG - Bulgaria and CBN (an agency for sociological surveys and projections in the IT area) traditionally offer that kind of information. Data from their surveys are presented in the following tables (Tables 9 and 10).

Table 9. ICT market in Bulgaria, 2001-2003 (EUR Million)

	2000	2001	2002	2003
Servers	21	28	35	37
PC	54	61	66	71
Office equipment	18	19	20	21
Communication equipment for end customers (cell phones, etc.)	50	66	68	70
Network equipment	188	269	321	335

(continued)

Software	25	28	33	39
IT services	36	39	43	50
Total IT	214	244	271	298
Total telecommunications	841	1056	1207	1301
Total ICT	1055	1300	1478	1599
Growth, %		+23.2	+13.7	+8.2

Source: IDG research, www.idg.bg, November 2002

Table 10. IT business in Bulgaria
(only the top 250 IT companies are included)

	1998	1999	2000	2001	2002
Total revenues (thousand USD)	204 231	272 390	313 348	391 685	415 200
Growth, %	+40.9	+33.4	+15.0	+25.0	+6.0

Source: CBN data published in Infoweb, www.infoweb.bg, 2002 prognosis

There are differences in the figures of the above two tables which might be explained most probably with the different methodologies used by the two companies, as well as with the sample of companies covered by their surveys. At the same time the market growth rate indices are almost the same which indicates that this is the true picture of ICT business in Bulgaria during the recent years.

At the end of November the **First International Conference on the European Experience in the Introduction of e-Government was held in Sofia**. The conference was organized by the Bulgarian Association of Information Technologies (BAIT), the Institute of Public Administration and European Integration and the Development of Communications and ICT Agency at the Ministry of Transport and Communications. The Information, Communication and Management Technologies Coordination Center that underlay the Bulgarian e-Government Strategy developed and approved by the Council of Ministers, supported the conference, too.

The idea behind holding this conference was to support the Bulgarian government in the development of e-government by promoting its essence and discussing the possibilities for its establishment and successful implementation. More than 30 reports were presented at the forum by well-known and acknowledged experts in the field, as well as by leading Bulgarian companies experienced in developing projects related to the provision of IT services. Almost 150 public administration servants and NGO representatives involved in the establishment of e-government participated in the conference.

Regional telecommunications symposium on the Development of the Reform in the Telecommunications Sector and its Impact on South-Eastern Europe took place on 2 and 3 December 2002 in Sofia. The forum was held under the auspices of the Ministry of Transport and Communications and with the financial support of the European Commission. The South-Eastern European Institute for Telecommunication

and Information Research (INA), the Ministry of Transport and Communications and the Communications Control Commission were among the organizers of the symposium.

The trends of development in the telecommunication sector in Europe and its influence over South-Eastern Europe were discussed at the symposium. Ministers of transport and communications from the region - Greece, Turkey, Macedonia, Serbia, Bulgaria, Romania, Albania, consultants on telecommunications, as well as leaders of national telecommunications regulators made presentations at the symposium.

The Communications and Information and Communication Technology Development Agency at the Ministry of Transport and Communications and the Bulgarian Association of Software Companies (BASCOM) signed with the European Software Institute (ESI, Spain) tripartite **memorandum for establishment of a Regional Center for Improvement of Software Companies in Sofia (ESleCenter)**.

Before Bulgaria ESI has established two other regional centers in Brazil and China. The fact that our country was selected for the establishment of a similar e-Center is an indication for the high evaluation of the potential and condition of the Bulgarian software industry. The idea of the Bulgarian center is to help companies from the country and the region by assisting them in applying new technologies and organization of the operations, as well as in reaching world quality standards.

The work of the center will be aimed at:

- improving the quality of products and services in the software development area at the domestic and regional market; applying and promoting "good practices";
- improving and consolidating the links between universities and the industry by providing opportunities to highly qualified specialists, securing professional experience for the graduating students and work on projects using modern technologies;
- providing independent methodological and organizational assistance for the development and monitoring of software projects of national and regional importance;
- initiating long-term projects in new technology areas that will be beneficial to all participants - the government, industry, universities and all other stake-holders.

At the end of 2002 the Ministry of Education presented **a draft of a Strategy for Introducing ICT in high school**, the objective of which is to lay the foundations for creating "a system for ICT education that allows unrestricted development and its application in the overall high school curriculum". Besides major guidelines, the draft document includes an operational plan which presents in details the tasks and the time frame that should be observed for the implementation of the Strategy.

Number of Tourists and Revenues from Tourism

Tourism in 2002 was one of the most dynamically developing sectors of the economy. Despite the general unfavorable trends in worldwide tourism development, both the number of tourists to Bulgaria and revenues from tourism increased. According to data from the Ministry of Economy **last year the country was visited by 2 992 590 foreign tourists. This is by 8.6 per cent more compared to the previous year.**

A significant change is observed also in the last quarter of the year – in December, the start of the winter season, the number of tourists was by 22 per cent more compared to December 2001.

Revenues from tourism in the fourth quarter of last year reached USD 183.4 m versus USD 151.1 m for the same period of the previous year. Only in December revenues amounted to USD 63.6 m, which is by USD 20 m more than December 2001. **The balance in tourism (net revenues) in the fourth quarter is USD 41.6 m versus a balance in the last quarter of 2001 of USD 23 m.** These data justify the optimistic expectations of a good winter season.

In support to the reported data there are some facts and projects directed towards improvement of the conditions in winter resorts (general and special infrastructure) the implementation of which was declared or started at the end of last year. Such improvements are the first ski runs with artificial snow and lighting in Borovets, completion of the construction of a gondola lift in Bansko and the new ski runs and facilities there. Once again the decision on renovation of the Romanski lift in Vitosha mount was announced and this project is expected to be completed in 2003 – 2004. Its successful implementation will allow to raise the lift's capacity from 600 to 2400 persons per hour. Other projects announced at the end of last year, envisage the construction of a modern ski center at Chepelare to link this town to the resort of Pamporovo. Most probably, some of the funds will be provided under SAPARD and ISPA programs. There exist some possibility for implementation also of Sutka Project – a ski center near Velingrad.

The implementation of the aforementioned projects is expected to resolve one of the major problems of Bulgarian tourism – diversification of its monocultural nature (focusing on specialized infrastructure in sea coast resorts). These projects are aimed at enlargement and renovation of specialized infrastructure in winter resorts, too, to extend the skiing season, and to add new ski centers (Velingrad and Chepelare) to traditional winter destinations (Bansko, Borovetz, Pamporovo).

Regulatory Framework

As of 1 October 2002 the **new Tourism Act** entered into effect. It regulates in detail the relations between tourists and tour

operators or agents. The Act alleviates the licensing regime by repealing licenses for restaurant and hotel running but keeping the ones for tour operator and tour agency activities. The Act outlines also the role of local governments for the control and development of tourism on local level.

Several **regulations to the Act** became effective, too – the Ordinance on Categorization of Tourists Sites, the Ordinance on Licensing of Tour Operators and Tour Agents, as well as the Tariff of Charges collected under the Tourism Act.

Higher requirements are introduced for categorization of tourist sites. Due to problems arising with tour operators licensing in December the Ministry of Economy made a decision to postpone for 6 months (by 1st July) the enforcement of art. 14-18 of the Ordinance on Licensing of Tour Operators and Tour Agents which impose high requirements towards the number, qualification and experience of the staff, as well as to offices and their equipment.

After 1 January 2003 tour operators must also offer insurance contracts under another regulation to the law. **The lower rate of VAT for companies operating in the tourist sector is preserved – these will pay 7 per cent VAT on tourist services.**

Work continued on the development of a **National Strategy for Development of Tourism**. In the course of development is also a **National Strategy for Development of Eco-tourism** which is expected to be completed in 2003. Representatives of the ministries of economy, the environment and agriculture are involved in its elaboration. The idea is to make the country a leading destination for alternative tourism among Southeast European countries and to encourage development of European transnational eco-tourist routes.

A decision was made in the fourth quarter to set up an **Executive Agency for National Tourism Promotion and Information** as a legal entity funded from the national budget. This agency is going to implement the National Promotion Program adopted by the National Tourism Council. It will set up and maintain a national electronic system for tourist information, it will coordinate the presentation of Bulgaria as an attractive tourist destination abroad.

In November Bulgaria took part for the 23rd time in the International Tourist Exchange in London. There, Bulgarian and foreign tour operators stated that in their offers for Bulgaria in future they were going to rely on high quality and attractive prices.

In October representatives of 28 tour operators and companies from Germany, specialized in eco-tourism, presented to municipalities from the Southern Black Sea Coast their opportunities to support eco-projects in this region. The

first **national eco-tourism** forum *Eco-tourism, Mountains and Protected Territories – Partners for Welfare* was held in the beginning of October. The major points of the future Eco-tourism Strategy were presented at this forum. It was announced that in 2003 the PHARE program will fund projects for development of eco-tourism at the amount of about EUR 7 m; the same amount is expected to be invested in cultural tourism, too.

State of the Sector

The share of the agrarian sector in Bulgarian economy preserves a downward trend. After the strong third quarter when by tradition this share reaches its peak values for the year, in the fourth quarter agriculture accounts for around 11.5 per cent of GAV and 10 per cent of GDP. Insofar as land consolidation and census are not a fact yet, one cannot speak of change in the number or size of available farms. The employed in the agrarian sector are not fully covered by the statistics, either, and there is significant discrepancy of estimates. Winter crop sowing is given a positive assessment; the contracts signed between the State Agriculture Fund and farmers for subsidies to purchase seeds, fertilizers and diesel fuel also reveal that planted areas will remain at least at the level of the previous year, and higher yields and better quality of farm products could be expected. As of end of November wheat areas were more than 8 million decares, and barley areas - 2.7 million decares.

Trade dynamics is most indicative of the sector's state and development. Government measures such as intervention on the grain market, set up of a wheat commodity fund, and financing of export-oriented grain producers proved effective. The grain market recovered, and the 2002 growth in the export of farm products is expected to exceed 10 per cent. Exported barley of the 2002 crop amounts to 552 000, or twice the amount for the whole 2001. Exported wheat of the 2002 crop amounts to more than 600 000 tons (with 824 000 tons of the 2001 crop), and the exported sunflower of the 2002 crop amounted to 200 000 tons (with 91 000 tons for the whole 2001). The foreign trade in farm products balance remains positive and preserves an upward trend.

The projects implemented under the SAPARD Program are indicative of the development perspectives in the sector - the three SAPARD commissions organized in the fourth quarter of 2002 approved another 69 projects amounting to a total of over BGN 52 million. As at year end the funds utilized under the program amounted to more than BGN 30 million; they were spent for the implementation of 118 projects, which were completely finalized by that moment.

Environment for Development

There was a speed up of the work on harmonization of legislation in the field of agriculture in fulfillment of the task to accelerate negotiations for accession to EU. During the quarter under review the National Assembly passed **amendments to the Farmers Support Act**, which regulate government support to farmers and the implementation of the measures incorporated in the National Plan for development of Agriculture and Rural regions aiming at the set up of efficient farms and competitive food industry, restructuring of Bulgarian agriculture in accordance with European market requirements, ensuring

employment of the population and gradual replacement of imported raw materials for the needs of the processing industry with Bulgarian ones.

According to the Act, direct subsidies will constitute the major fiscal instruments, including current, investment and export subsidies, long-term lending under three investment programs, and intervention on the market of farm products. The tasks of the State Agricultural Fund are also approved by this Act: to provide financial support to farmers; to perform the functions of a SAPARD Agency; to intervene on the markets of farm products by way of buying out unprocessed commodities at intervention prices; to grant export subsidies to exporters of unprocessed and processed agricultural commodities with a view to encourage the production of quality commodities for export. The basic objective is to restructure Bulgarian agriculture and achieve competitiveness in accordance with European market requirements, as well as to ensure employment of the population by way of promoting Bulgarian and not imported raw materials for the processing industry.

Farms fragmentation remains a major barrier to the set up of efficient agriculture, to making full use of the measures to support producers and attract foreign investments. Amendments to the Ownership and Use of Farm Land Act and the Regulation on the Terms and Procedure of Fixing Current Market Prices of Farm Land. Small and fragmented farms¹² impede and production and make it more expensive. A Consolidation by Agreement Project was started in two specially chosen territories with the cooperation of the Dutch cadastre agency. According to project terms, the agreement of owners and users is required to consolidate farm land, as well as availability of equal terrains and equal category of farm land. Land from the State Land Fund may be used to support the consolidation process. This land shall be used in exchange of land of owners restored to them in other municipalities and regions. Owners of newly set up estates shall not have the right to fragment their land to plots smaller than the consolidated plot fixed for the corresponding territory.

During the quarter under review the Government approved another two acts directly related to the negotiation process - Amendments to the Stock-breeding Act and a new Act on the Census of Bulgarian Farms. **Amendments to the Stock-breeding Act** are related to both the need to consolidate farms and set up modern farms having capacity to produce quality commodities, and the development of stock-breeding in compliance with environmental standards. A special chapter of the Act protects the national gene pool; the Government will grant subsidies for production and storage of genetic material, and valuable animal breeds will be raised in pedigree farms. The Act covers sub-sectors which were not covered before,

¹² According to data by MAF, owners of farm land currently amount to 2 million people, and the land is fragmented into more than 25 million plots.

such as apiculture, sericulture, rabbit-breeding; these become increasingly important and will play an important role in the future restructuring of the sector. An important amendment to the act constitutes the introduction of the European system of qualification and classification of animal products in slaughterhouses (EUROP), which will encourage the supply of quality meat for production of quality products for the market.

The Act on the Census of Bulgarian Farms, which sets forth 1 July 2003 as a starting date of the census, is of paramount importance for the process of negotiations on Chapter Agriculture, because the amount, scope, and orientation of direct subsidies and payments in the agrarian sector will be dependable on that. The plan is to complete the census by 30 November 2003, and to summarize final survey results by September 2004. Thereby Bulgaria will fit in the approved time limit for carrying out full census of farms in EU candidate countries from 2002 up to 2004.

Negotiations with EU on veterinary and phyto-sanitary inspection were finalized in the beginning of December. One fourth of European agriculture-related legislation is devoted to these problems. The most important element of the negotiations in this field concerns the arrangement of transitional periods for producers of different kinds of agricultural commodities to gradually conform to requirements and achieve European standards. Increase of EU financing has been negotiated with a view to successfully implement European legislation in the field of veterinary and phyto-sanitary inspection. Difficult negotiations to arrange Bulgaria's agricultural quotas after the country's accession to EU lie ahead.

The 2002 positive trends continued through the last quarter of the year as well: the stock exchange trading in compensatory instruments (after its launching in September) was active, the SOFIX index raised, and the market capitalization also increased considerably in the last quarter of 2002. All the foregoing, combined with improved liquidity particularly of some types of securities included in the index, is considered to be an indication also of improved public companies' indicators, corporate management upgrading, or at least of market adjustment of the prices of the Bulgarian shares that used to be underestimated for many years.

In spite of all that, however, the capital market role in Bulgaria's financial sector remains insignificant in general – as of the end of December 2002 the total market capitalization of the Bulgarian Stock Exchange – Sofia AD was a little over 4 per cent of the updated estimate (as per the Ministry of Finance assessment) of the 2002 GDP. The capital market underdevelopment is explained both with the condition and prospects of the Bulgarian economy as a whole, and the fact that the mechanisms of financing through this alternative non-banking environment remain unfamiliar or not preferred even in the cases when relevant projects are available. **Liquidity remains low, the market does not promote the good corporate management practices, and the investment alternatives remain limited.** Financial intermediation continues to be carried out mostly through the banking sector.

The Capital Market as Shown by the Indicators of the Bulgarian Stock Exchange - Sofia AD (the compensatory instruments market excluded)

As of 31 December 2002 the market capitalization, according to data from the exchange, was a total of BGN 1,375,184,361 (of which BGN 252,873,237 on the official markets), while as of the end of the third quarter of 2002 the market capitalization was a total of BGN 1,025,580,832 (of which BGN 212,630,824 on the official markets). The turnover in the last quarter of 2002 was BGN 78,920,404 with traded 14,599,104 securities (this turnover and traded volume do not include the compensatory instruments and rights traded on the exchange for the first time, but include the block transactions, again excluding compensatory instruments). The SOFIX index continues to increase: as of June 30 it was 132.15, while as of 30 September it was already 149.82, and as of 31 December 2002 it was 183.08.

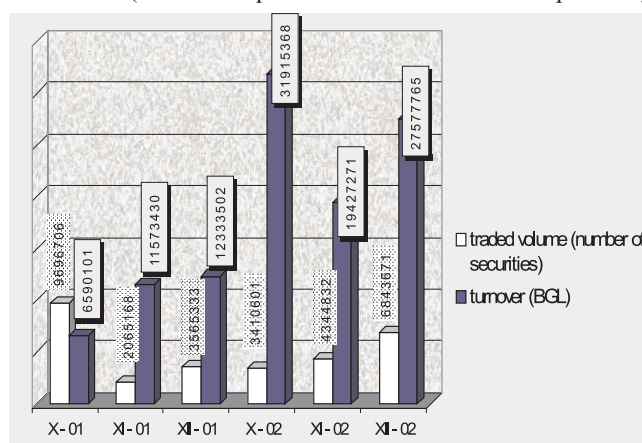
Thus **the last quarter of 2002 was undoubtedly positive in terms of the main indicators characterizing the capital market condition in Bulgaria** (which is measured traditionally and interpreted by means of the indicators from the Bulgarian Stock Exchange - Sofia AD). Excluding the compensatory instruments, but including block transactions, the exchange turnover and the traded volume in the quarter under review

exceeded those in the preceding quarter. The market capitalization and the SOFIX index also considerably exceeded the values as of the end of September 2002.

The serious shortcomings of the capital market, however, still remain in existence. The increased turnover in the last month of the year is due partially to transactions aiming solely and only to achieve a certain taxation effect. Although liquid positions such as Biovet AD and Sofia – BT AD marked a considerable growth in prices in the last quarter and attracted the investors' attention, they are not included in the SOFIX index. The latter fact challenged again the capacity of the SOFIX index to reflect the state of the market correctly.

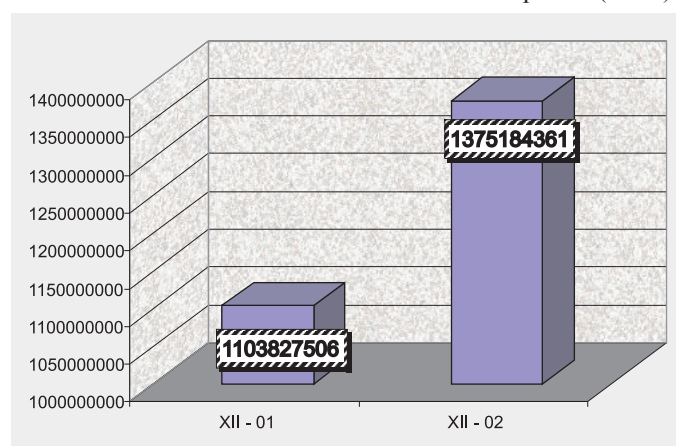
Low liquidity is one of the problems, which continue to be characteristic of this market – for example, in December over 40 per cent of the official shares market turnover was due to two transactions (with shares of Eurohold AD). The conclusions are contradictory also if comparisons to the end of the preceding year 2001 are made. Concerning turnover, trade on the Bulgarian Stock Exchange - Sofia AD in the last quarter of 2002 marked a positive development compared to the same period of the previous year (an increase more than twice), however, the traded volumes in the same period declined although inconsiderably (See Figures 15 and 16). **Generally, decreased or maintained volume with increased turnover continues to be the manifestation of the trends for property consolidation and trade concentration on a smaller number of issues, while on the other hand the liquidity of the larger part of the listed securities declines or remains low. The past quarter, however, marked good liquidity especially of some of the securities included in the calculation of the SOFIX exchange index, which is a fact deserving positive assessment.**

Figure 15. Trade on the Bulgarian Stock Exchange - Sofia AD (the fourth quarter of 2001 and 2002 respectively)



Source: Data of the Bulgarian Stock Exchange - Sofia AD, monthly bulletins

Figure 16. Market Capitalization on the markets of the Bulgarian Stock Exchange - Sofia AD as of the end of the period (BGN)



Source: Data of the Bulgarian Stock Exchange - Sofia AD, monthly bulletins

In the last quarter of the year the nine-month reports of public companies were expected, which were due in compliance with the law amendments made in mid-2002. As it had happened in previous periods, too, a number of companies failed to submit their reports in due time, which **reconfirmed the problem, which requires upgrading of the accounting and regulatory practices and the principles of corporate governance.** This gives grounds to conclude that **the dependence of the listed companies' prices on the publicly announced corporate events on the Bulgarian market remains quite contradictory.**

In the fourth quarter of the year there was no intensification of **the bonds market** on the Bulgarian Stock Exchange - Sofia AD. The bond issue of Sliven municipality was registered for secondary trading on the Stock Exchange. Nevertheless, totally for the quarter on the official markets of the Bulgarian Stock Exchange - Sofia AD only 18 transactions with corporate bonds were concluded with a total turnover of less than BGN 6 million. On the non-official markets of the exchange totally for the quarter there were 21 transactions with corporate bonds, while the total turnover was a little over BGN 8 million. In the beginning of November the subscription was launched for marketing of the biggest issue of corporate shares in Bulgaria by now (of Overgas AD of BGN 20 million face value), but this was effected out of the exchange under private marketing conditions. A registration for secondary trading on the exchange is expected (similarly to the procedure conducted in the beginning of 2003 with the newly issued and successfully marketed corporate bonds of AutoBohemia AD).

For the first time on the exchange in the 2002 fourth quarter there was **an auction for the sale of rights** (unexercised rights to a new issue of Sviloza AD). Regardless of the inconsiderable volume this new practice is being successful and it confirms the potential of the trading mechanism of the Bulgarian Stock Exchange - Sofia AD. Sviloza AD was the first public company,

which increased its capital through issuing of negotiable rights. The binding requirement to the issue of rights in case of increase of capital was stipulated in the amendments to the Securities Public Offering Act made in the summer of 2002, the idea being to better protect the interests of the small investors. Two more companies increased their capital in November and issued rights to investment in that increase. The auction of unexercised rights was held in early January 2003.

At the end of November the Board of Directors of the Bulgarian Stock Exchange - Sofia AD accepted for trading on the non-official market the shares of **the second in Bulgaria opened investment company** (Elana Eurofond AD).

Trade in Compensatory Instruments, Stock Exchange Privatization and Statutory Framework Development

The start of the trade in compensatory instruments on the floor of the Bulgarian Stock Exchange - Sofia AD was undoubtedly among the leading events on the capital market throughout the whole year 2002. The positive expectations have been met by now, as it is clearly evident from the fourth quarter of 2002 (which was the first full quarter having such trade).

At the end of August the Board of Directors of the Bulgarian Stock Exchange - Sofia AD passed a resolution for registration of the compensatory instruments (on the Non-official Market, Compensatory Instruments Market Sector). The trade started in the three issues of bonds, which comprise the group of compensatory instruments in compliance with Compensatory Instruments Transactions Act – these are compensatory bonds under the Act on Compensation for the Owners of Nationalized Property, and the personal compensation bonds under the Act on Ownership and Use of Agricultural Land, and the Act on the Restitution of Ownership over Forests and Forestry Fund. The Compensatory Instruments Transactions Act, which was adopted earlier in 2002, suspended the issuing of, transactions and payments with such instruments pursuant to the previously applied order. After a certain delay and failure to meet the initial deadline set by the law, on 2 September 2002, the trade in compensatory instruments started again. From that moment on transactions with compensatory instruments are conducted only on the floor of the stock exchange.

The statistics for October – December 2002 show the following results: a total of 5,519 transactions with compensatory instruments were performed with turnover BGN 33,800,975. Apart from these, block transactions with compensatory instruments were also registered on the exchange, namely: 14 transactions with compensatory bonds with total turnover BGN 6,257,341 and 25 transactions with a total turnover of BGN 13,067,773. During the period the compensatory instruments were at a price of 19 to 27 per cent of their face value, and the price was at an average decrease over the 3-month period.

While compensatory instruments trade was lively and recovered the interest in the potential of the organized capital market, particularly the **lack of clarity specifically regarding the exchange privatization** cast a doubt on the prospects, at least in the mid-term, of revival on the capital market in Bulgaria.

In July 2002 the annual list of 1,073 companies for privatization against non-cash means of payment was adopted; this fact did not allow for making firm forecasts regarding the occurrence of new companies to be traded on the Bulgarian Stock Exchange - Sofia AD. The two main reasons for the latter were: First, the procedure for making those companies public was obviously going to take a long time. Second, there still existed concerns about further changes in the list of companies for privatization against compensatory instruments and investment bonds (including the part of the list referring to the privatization through the exchange).

These concerns prove out justified for the time-being. At the end of September the Privatization Agency passed a decision for determining the public offering as a method for the privatization of 85 companies (mostly minority blocks of their shares). It was envisaged that these companies would be grouped and sold in pools. This fact actually constituted a reduction of the initial list for privatization through the exchange and therefore it was received with disappointment by the financial community. Afterwards, giving various grounds, some pools were taken off the list of the 85 companies, and this caused uncertainty in the expectations from the exchange privatization. Especially negative response came from the owners of compensatory instruments.

As of the end of the year the Privatization Agency reported that procedures had been initiated for 11 pools of minority blocks of shares of approximately 90 companies, which will be traded against compensatory instruments. Investment intermediaries were selected for 5 of them, and again at the end of the year shares of 17 companies were registered on the floor of the Bulgarian Stock Exchange - Sofia AD. Regretfully, in the beginning of 2003 the marketing of the first pools for privatization showed that another problem existed, too: there were cases when the intermediaries were the successful bidders at the Privatization Agency tender and undertook an obligation for a high minimum sale price, while afterwards they failed to sell at this price and the sale was considerably delayed¹³.

In the second half of 2002 there was strong interest in the expected tender for selecting a consultant and investment intermediary for the stock exchange sale of shares of one of the companies most attractive for portfolio investors; this tender was completed in October. The pool contained stocks (from 12.8 to 49 per cent) of the State Insurance Institute – DZI AD,

Bulgarian Maritime Navigation EAD, Petroleum and Natural Gas Exploration and Extraction EAD, Bulgartabak Holding AD, and BTC (Bulgarian Telecommunication Company) EAD. However, despite the selection of a consultant and intermediary – perhaps with the exception of Petroleum and Natural Gas Exploration and Extraction EAD (which has already been made public and listed on the stock exchange in December) - the ambiguity about the other shares in the pools remains in place even today. The discussions regarding the large privatization transactions, including some of the companies in the pool, have not given any clarity at present about the privatization of shares of the aforementioned companies particularly by means of public offering on the exchange.

An addition to the topic about the progress of the privatization through the Bulgarian Stock Exchange - Sofia AD and of the expectations about fostering the capital market was also the procedure for the sale of 72 per cent of the capital of Sveti Sveti Constantine i Elena AD, Varna. This privatization was expected with strong interest insofar as the plan was a majority share to be sold for the first time on the stock exchange against compensatory instruments (and not through a more general sale by means of public offering on the exchange). The very sale of this block through the stock exchange was performed in three stages and was completed in mid-January 2003. Despite the delay in selecting an intermediary and hence, a delay in the privatization of this company, the buyers' interest resulted in stirring the market of compensatory instruments (required for the purchase of the block being sold) and therefore, in consuming a large resource (approximately 8 per cent according to most of the estimates) of the compensatory instruments available in circulation. The successful completion of this transaction, however, gave rise to other questions. First, disputes occurred about the restriction on the very procedure of sale, according to which the majority share should be sold combined in one whole indivisible lot in the last stage. This strongly limited the possibility for direct individual participation of a number of investors. Second, the delay (for example, lagging behind the schedule announced in the beginning of 2002 in the Program for Development and Encouragement of the Capital Market in Bulgaria) and the lack of clarity about the lists of companies for stock-exchange privatization are a confirmation of the concerns as to whether there will be sufficient and attractive blocks (especially ones beyond the above described first pools of the Privatization Agency).

Concerning the **statutory framework**, the fourth quarter of 2002 faced a development relating to the **Companies with Special Investment Purpose Act and the Financial Supervision Commission Act**.

The first draft was passed at first reading on 1 October 2002. The hope is that it will make a serious breakthrough in the environment for the capital market development in Bulgaria – both in connection with the possibility for emergence of the

¹³ See the interview for the *Pari* newspaper with L. Lekov, analyst at the Investor.bg.: *The Lessons from the Failure with the Zlatni Pyassatsi Pool*, 7 February 2003.

companies with special investment purpose mentioned above, and more generally, with the introduction of landmark norms in Bulgaria about assets securitization. The establishment of investment alternatives and the encouragement of joint investment schemes are mentioned as additional grounds for the draft. Discussions are still underway.

The draft of the Financial Supervision Commission Act was adopted also at second reading in the beginning of December. The draft concerns the unification of the supervision over the non-banking financial sector in Bulgaria: capital market, insurance and social security of the fully funded type. The costs reduction, the reduction of the existing administrative staff and the efficiency improvement are the major grounds behind the idea for integrating the supervision. Meanwhile there were intensive discussions both on the very essence of the idea for a unified supervisory body, and on removing the existing draft shortcomings of legal and technical nature, which would possibly be an impediment to the current regulatory and supervision practice or the future establishment of the new supervision regime.

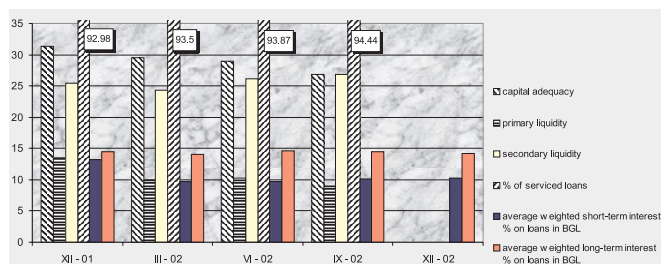
By President's Decree the passed Act was returned for reconsideration. The justification of the President's veto restated the most widely spread arguments of the draft law opponents in the last months. The President challenged the draft provision that the decisions of the Financial Supervision Commission would not be subject of appeal in court, and he also challenged some of the provisions regarding the annual fee, which the persons subjected to supervision will have to pay to the uniform financial regulator. The draft law was passed again by the Parliament in January without any changes.

The banks in Bulgaria maintain their stable condition, their excellent indicators of capital adequacy and liquidity, and their well operating bank supervision. As of the end of December 2002 there were 34 banks in Bulgaria; 27 of them are banks licensed to operate in Bulgaria and abroad, one bank has a license to operate in Bulgaria only, and there are six branches of foreign banks. In the last quarter of 2002 the number of banks decreased after the actual merger of HFB Bulgaria with TB Biochim.

Banking System Indicators

According to BNB data, as of the end of December 2002 the banking system had assets amounting to BGN 14,557,124,000, while at the end of September they amounted to BGN 13,475,455,000 (which is an increase of BGN 1,081,669,000 for the last quarter of 2002). At the end of December the deposits totaled BGN 11,282,160,000, while at the end of September they were BGN 10,527,760,000 (an increase by BGN 754,400,000 during the fourth quarter). The current profit of the banking system in December was BGN 266,625,000, while in September it was BGN 201,740,000, and in June 2002 it was BGN 132,715,000. In the last month of 2001, however, the current profit of the banking system was BGN 319,375,000. According to the latest available data from the BNB the capital adequacy of the commercial banks as of the end of September 2002 was totally 26.84 (group five excluded), while it was 28.98 per cent at the end of June (and 31.32 as of the end of 2001). At the end of September 2002 the primary liquidity for the banking system as a whole was 9.03 per cent, and the secondary liquidity was 26.88 per cent (these indicators were 10.27 and 26.15 per cent at the end of June respectively, and at the end of 2001 – 13.47 and 25.47 per cent respectively). These indicators are shown in Figure 17.

Figure 17. Some Banking System Indicators (%)



Source: data from the BNB, monthly information bulletins

Thus the banking system as a whole continued increasing its assets and deposits, as well as its current profit in the last quarter of 2002. The banking system current profit was increasing throughout the whole 2002, however in December it was still smaller than that in the last month of 2001. This is explained to a large extent with the accounting and reporting of the costs for provisions for losses from lending; therefore it does not give direct information about the system development. On the other hand, however, the ratio of net revenues from interest

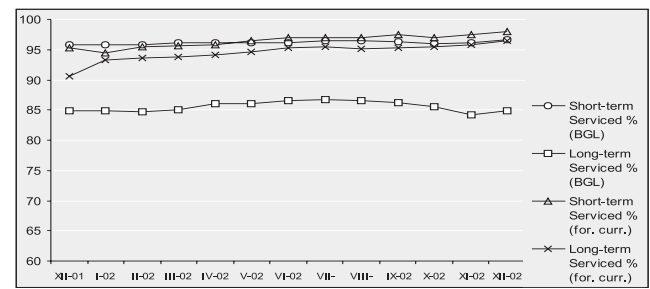
to other non-interest revenues decreased inconsiderably (from 2.30 to 2.25 at the end of 2001 and 2002 respectively, while at the end of 2000 it was 2.18), which indicates underdevelopment and insufficient diversification in the banking activities. The capital adequacy indicators as of the end of September were lower compared to both the end of June 2002 and the end of 2001; nevertheless, they are relatively quite high and are an evidence of the system stability. The banking system liquidity indicators in total for September show multi-direction fluctuations after the end of 2001 (the primary liquidity ratio decreases, but that of secondary liquidity increases), but they are still relatively high. All the aforesaid can be interpreted as an indication that stability is in place in Bulgaria's banking system, but the short-term trends are contradictory, and the banking system remains insufficiently effective, and underdeveloped. This conclusion can be confirmed to a certain extent also by the banks' lending activities review below.

Lending

In the absence of many of the products and services offered by similar institutions in the West, the lending activity has to be considered as one of the key indicators of the Bulgarian banking system development and of its efficiency. **Lending to the non-governmental sector shows a clear trend of increase** (under the Currency Board regime this is lending to commercial banks, which includes lending to non-financial state companies, private enterprises, households and non-banking financial companies). From BGN 4,374,627,000 at the end of 2001 the receivables from lending to the non-government sector reached BGN 6,250,741,000 at the end of December 2002. The newly agreed lending from commercial banks in 2002 amounted to a total of BGN 5,189.7 million, while in 2001 the newly agreed loans were totally BGN 3,084.21 million (growth of 68.27 per cent).

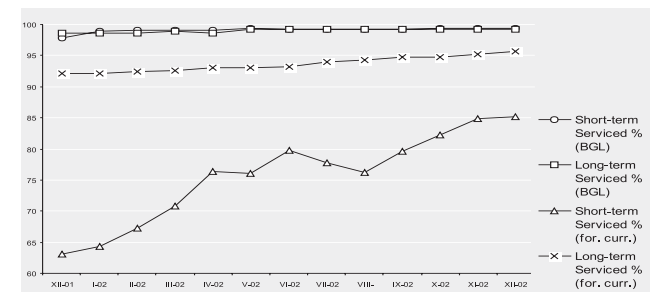
The state of the loan portfolio is also improving: at the end of 2001 92.98 per cent of all categories of loans in the banking system were performing, then at the end of June 2002 93.87 per cent were performing, and at the end of September 2002 – 94.44 per cent (Figure 17). This general conclusion holds true also particularly for the receivables from loans to private enterprises and households. Perhaps with the exception of receivables from enterprises under long-term lending in Bulgarian Levs, the percentage of performing loans compared to the respective group of loans was either increasing, or remained high in 2002 (Figures 18 and 19).

Figure 18. Loan Portfolio Condition: Private Enterprises



Source: data from the BNB , cash report, and own calculations

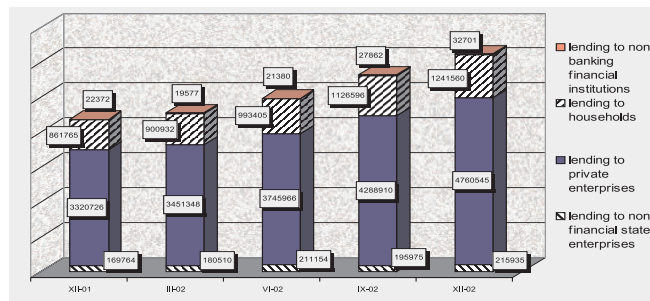
Figure 19. Loan Portfolio Condition: Households



Source: data from the BNB , cash report, and own calculations

The interest rates on short-term and long-term lending in Bulgarian Levs dropped in December 2002 as compared to the end of 2001, this being better manifested with short-term lending. The latter, however, increased inconsiderably in comparison to the end of September 2002 (See Figure 17 again). The lending dynamics shows some other interesting short-term trends (with regards to currency, term and borrowers). For example, the review of the receivables from lending to the non-government sector shows the biggest increase of lending exposure both to private enterprises and to households; however their relative share remains practically unchanged (Figure 20).

Figure 20. Receivables from Loans to the Non-Government Sector (In Thousand BGN)



Source: data from the BNB , monthly information bulletins

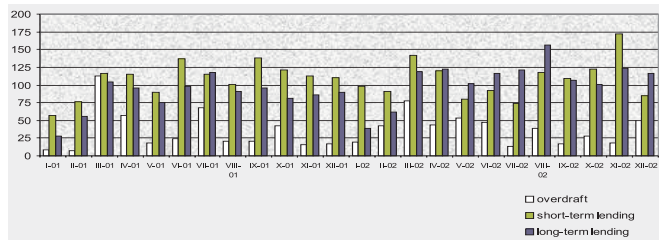
Figures 21, 22 and 23 show the dynamics of the newly agreed lending in 2001 and 2002. In particular, the newly agreed loans in the last two months of 2002, similarly to the same period of 2001, manifests an increased lending activity and confirms the trend of general increase of extending loans, especially

compared to 2001.

Concerning the terms of loans another interesting trend of the last months of 2002 is the increase of the share of long-term loans compared with short-term ones in BGN and Euro. This fact reflects not that much the dynamics of the interest structure, but rather an increase in the investment activities in the country and the taking into account of the currency risk (under the currency board conditions and the Euro as a reserve currency for Bulgaria). In the fourth quarter of 2002, probably due to the decreasing US dollar exchange rate, the newly agreed short-term loans in dollars exceed that of the preceding quarter.

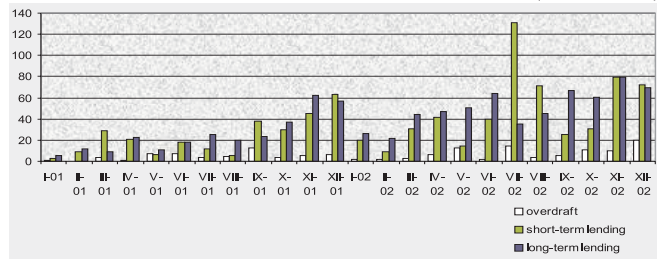
The bank lending can be interpreted in terms of the conditions and prospects of Bulgarian economy as a whole, and particularly regarding the existence of attractive investment projects. With the development of the economy and the emergence of concrete projects, alongside with the expansion of competition and efficiency in the banking sector itself, a continued increase of the long-term lending to the private sector may be expected. **The increase of lending to households in 2002 is a clear indication of the further development of retail banking as well. Despite the objective indicators of the sustainable trend towards increased lending activity, at present there prevails the assessment that there is a still larger potential for lending, including to small and medium-size enterprises, as well as for diversification of the activities. Bulgaria's banking system is stable, but it is still inconsiderable in terms of assets volume and portion of the lending in the GDP.**

Figure 21. Newly Agreed Lending from Commercial Banks - in BGN (BGN mill.)



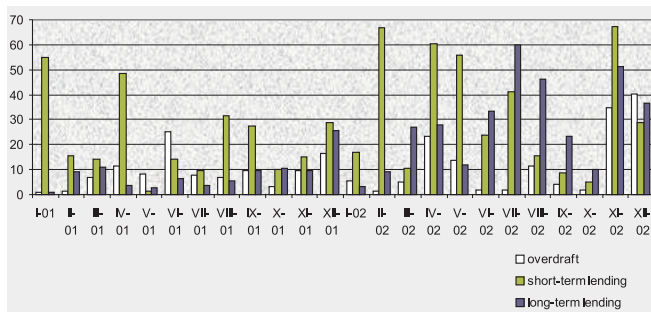
Source: data from the BNB , monthly information bulletins

Figure 22. Newly Agreed Lending from Commercial Banks - in EURO (BGN mill.)



Source: data from the BNB , monthly information bulletins

Figure 23. Newly Agreed Lending from Commercial Banks - in USD (BGN mill.)



Source: data from the BNB, monthly information bulletins

Restructuring and Privatization in the Sector

Through various channels, such as privatization, opening of representation offices, branches and newly established banks, **the foreign participation in Bulgaria's banking system is already prevailing both in equity control and managed assets.** According to the data quoted by the BNB¹⁴, private banks account for 79.6 per cent of the total banking system assets as of the middle of 2002. At that same time foreign banks and investors controlled 72 per cent of the banking assets.

In the recent months serious development has been observed regarding the privatization of the last two large state-owned banks, and the leading role here again belongs to the foreign investors and consultants. At the end of July the contract for the sale of TB Biochim AD to Bank Austria was signed; 99.59 per cent of the capital of TB Biochim AD was sold for Euro 82.5 million. The Bank Austria Kreditanstalt banking group had been present in Bulgaria by then through the group's subsidiary HFB Bulgaria. The buyer's plan was the subsidiary bank to be amalgamated with TB Biochim.

The TB Biochim privatization and the HFB Bulgaria acquisition were completed in the fourth quarter of 2002. Biochim shares were transferred by the Banking Consolidation Company to Bank Austria Kreditanstalt on 7 October 2002. At the end of November TB Biochim was transformed by acquiring HFB Bulgaria, where the latter terminated its activities without liquidation as a result of the acquisition. Then the capital of TB Biochim was also raised and the whole new issue was subscribed by Bank Austria. After this transaction Bank Austria's share of TB Biochim increased to 99.68 per cent. The transformation was announced accomplished at the end of 2002, and TB Biochim was then attributed a market share of 6.6 per cent and assets of over BGN 810 million. The latter placed the bank in the First Group of Banks according to the grouping made by the BNB. **After the privatization of TB Biochim, private banks in Bulgaria account for almost 85**

per cent, and foreign banks and investors for almost 77 per cent of the total assets in the banking system (according to data of mid-2002).

The last large state-owned bank is DSK Bank AD (State Savings Bank); the latter, together with the Encouragement Bank, account for the remaining 13.4 per cent of the state share of banking assets. In July five potential bidders were short-listed as consultants on the privatization of DSK Bank; from among these later on, on the basis of further presentations, J. P. Morgan was selected to be the consultant. The final contract with the consultant was signed in the beginning of October. Again in October, after the relevant amendments to the law, the state's share of 75 per cent of DSK Bank AD was transferred to the Banking Consolidation Company and thus it became possible for the sale of the bank to be ultimately finalized.

About mid-December 2002 it was known that five potential buyers had shown interest in DSK Bank. At the end of January 2003 the deadline for the submission of indicative bids by the candidate-buyers expired. Bids were submitted in due time by: the Austrian Erstebank, the Hungarian OTP, and the Greek Pireus Bank. Up to 100 per cent, but not less than 80 per cent of the bank's capital, was offered for the privatization of DSK Bank. Since all the three potential buyers promised to give a better price per share if offered 100 per cent of DSK Bank AD, the BCC decided that the whole block of shares would be offered for sale. The BCC decided further on that all the three candidate-buyers should be admitted to the pre-privatization study of DSK Bank.

Statutory Framework

The two draft laws for amendments to the Banking Act, which were submitted in March 2002, were passed in the third quarter of 2002, as well as the draft of the Banking Insolvency Act, which was put forward as early as in September 2001, and afterwards the amendments to the statutory framework continued also in the last quarter of 2002.

In December a group of MPs from the ruling coalition put forward to the Parliament a **new draft for amendments to the Banking Act**. The single proposal in this draft was a requirement to be put in place that at least one Bulgarian citizen should be elected a member of the managing bodies of a bank, and this member should be required to speak Bulgarian language and to have lived in Bulgaria for at least one year preceding his/her election. The draft is justified by the need of better communication among the commercial banks and official Bulgarian institutions, better adaptation to the Bulgarian market and better knowledge of the situation in the country. This justification stems from the concern of certain representatives of the banking circles in Bulgaria regarding the limiting of the Bulgarian bankers' access to senior management positions in banks, most of which are already under foreign control. The

¹⁴ Source: BNB report on the first half of 2002

draft is being considered.

A **draft on Amendments and Additions to the Bank Deposits Insurance Act** was also adopted in December. **The secured amount of deposits in banks was raised from BGN 10,000 to BGN 15,000.** The main grounds for such an increase was to achieve better compliance with the European directives and Bulgaria's commitment to have the depositors' security reach Euro 20,000 at the time of the country's accession with the European Union.

The two drafts on Amendments to the BNB Act put forward in June and July respectively, failed to be passed. These drafts were justified with the willingness to take counteraction against the resolution passed by the BNB for closing down three regional branches: in Rousse, Bourgas, and Vratsa. The issue about the regional branches of the BNB was one of the most widely discussed in the media in the summer of 2002, however, a legislative intervention proved out to be necessary. Eventually, the strong pressure resulted in a trade-off decision by BNB: in September the Managing Board of the BNB passed a resolution, wherein it partially revised its previous position – the regional branch in Vratsa was closed down, and the regional branches in Bourgas and Rousse were transformed into BNB representation offices, with no desk operations.

In the last quarter of 2002 **amendments were made also to bylaws.** Some of the more important ones are the following instruments issued by the BNB: Ordinance No. 9 (which substituted the one of 1997) for assessment and classification of the bank risk exposures and formation of provisions for losses due to devaluation; new Ordinance No. 5 (replacing the previous one of 1998) on the order and conditions for acquisition of, payment and trade in government securities; as well as Ordinance No. 15 on control over transactions with dematerialized government securities.

Social Security

In the last quarter of 2002 the main discussion regarding social security was related to the measures, which the Ministry of Labor and Social Policy (MLSP) is planning to implement from the beginning of 2003 for improving the collection rate of social security contributions and reducing the share of gray economy, namely: introduction of minimum insurance thresholds by economic activities and sectors, and mandatory registration of labor contracts at the National Social Security Institute (NSSI). In December the new Social Security Code was passed at first reading; it provides for the introduction of the above-described measures in the beginning of 2003. The NSSI budget for 2003, which was adopted in early December, received the negative assessment of the IMF with doubts about the implementation of the revenue side of the budget.

Two new obligations for employers were introduced at the beginning of 2003 with a view to better social security of employees, and a more competitive environment for business. These are obligations related to the Mandatory Registration of the labor contracts at the NSSI, as well as the observance of the minimum social insurance thresholds when paying social security contributions for persons employed under labor contracts and under contracts for management and control of commercial companies.

Two thirds of the **minimum social insurance thresholds** were actually negotiated between the employers' and trade-union organizations, while the remaining one third were specified through expert channels, again with the involvement of representatives of employers, trade unions and the government. According to NSSI the agreed amounts of the minimum insurance thresholds reflect the actual situation of labor demand and supply on the labor market. The standard Eurostat classification of economic activities, also used by the EU member states, is used; and the classification of professions used is based on a classification of the International Labor Organization. The effect of the new policies in the field of social security has been assessed to be approximately BGN 162 million, however certain fluctuations are possible, hence the risks hidden in the NSSI 2003 budget. It is expected that negotiations for determining the minimum salaries by sectors and professions will be initiated in 2003.

The highest social security contributions will be paid by the persons employed in the production of coke, refined petroleum products and nuclear fuel, financial intermediaries, bankers and managers of luxury hotels. The difference between the minimum thresholds and salaries is that in the former case social security contributions are paid based on the average salary for a profession, while in the case of the latter an amount is determined and no employee can be hired against a smaller remuneration.

The NSSI completed 2002 with a balance of unused state budget subsidies, which amounted to BGN 92-93 million.

An additional deficit is possible for 2003, indeed. The risk stems from the fact that the state budget subsidies are smaller, and also from the fact that there is an expectation for additional revenue to come from the implementation of new policies for improving the collection rate of the social security contributions, while the effect of such practices has not yet been tested in reality.

The Social Security 2003 Budget Act plans for revenues amounting to BGN 3,017 million, and expenditures of BGN 3,954 million. The difference of approximately BGN 940 million will be supplemented from the state budget.

A 2003 deficit of the Pensions Fund is planned amounting to approximately BGN 478,575 million, which results from the fact that the pension reform is still at a stage where the retirement age is slowly being increased and the number of pensioners is slowly decreasing, with simultaneously maintaining the actual value of pensions, and having even a small real growth every year. According to the preliminary estimates by the NSSI the deficit of the Pensions Fund is expected to be covered from own revenues from social security contributions in the period 2007-2008. Whether the NSSI forecast will be implemented depends on the impact, which the minimum social security thresholds and the Mandatory registration of labor contracts will have in the future on the collection rate of security contributions and the functioning of the labor market in general.

What is new is that starting from 2003 the government will pay the health insurance contributions of 1.5 million children of age up to 18 years. The state budget has allocated BGN 18 million for this purpose. Until now those children used to be ensured by an employed family member, who paid BGN 0.78 / per month per child. Starting from 2003 the government will pay BGN 1. **The minimum monthly amount of the insurance income for a self-insured person is changed from BGN 170 to BGN 200, and the maximum insured income – from BGN 850 to BGN 1,000.** The taxation burden for the Pension Funds remains unchanged. **The only new thing is the introduced 4-per cent contribution to the unemployment fund, which is to be paid on behalf of commissioned military staff.** **The minimum insured income of employees, who work at specialized enterprises, cooperatives and production workshops for people with impairments, is set at 50 per cent of that agreed for the respective economic activity.** The purpose of the latter measure is to mitigate the insurance burden of working people in disadvantaged position on the labor market, and also to encourage the employers to hire such people, the aim being better social integration to be achieved.

Until 2004 included the spreading of the social security contributions burden between employers and insured persons will remain at 75:25. Concerning the impact of the new social security legislation for 2003 on the business climate in Bulgaria the Bulgarian Industrial Association (BIA) sent an open letter to the Minister of Economy emphasizing that the amendments in

the social security legislation will have a negative impact on the employers because a cumulative negative influence of several factors is expected to overlap, namely:

- Maintaining for two more years the ratio of allocation of social security contributions between employers and employees;
- One more year delay in repealing the employer's obligation to pay social security contributions on compensations;
- Delay in repealing the payment by the employer for the first three workdays of a temporary disability period;
- Maintaining the situation where workers and employees under labor contracts are not on an equal footing with civil servants;
- Unsettled remains the matter about financing early retirement of commissioned military staff, Ministry of Interior employees and the other persons specified under Article 69 of the Mandatory Social Security Code.

In 2003 as a result of the action of the first four factors the employers alone are expected to suffer losses amounting to BGN 194 million. In spite of the employers' protest letter the MLSP decided to delay the introduction of the amendments to the social legislation that were promised to the employers; the main reason was the still not very efficient functioning of the labor market and the still low level of population's real income. The two new administrative measures taken by the MLSP, as well as the overall strategy in social policy, in the MLSP's opinion are aimed at one particular point: more orderliness and social fairness.

From the beginning of 2003 **employers are required to register the labor contracts** of new employees at the NSSI within 3-days. The existing labor contracts, on the other hand, should be registered not later than 30 April 2003. Within 3 days every employer will have to send the NSSI also a notification about any changes in the labor contract, which refer to the job position of the employee or the term of his/her labor contract. In case of labor contract termination the NSSI will have to be notified within 7 days. This has been stipulated also in the amendments to the Labor Code, which were adopted at the end of 2002.

An amendment to the Social Security Code stipulates that in the cases when a worker is hired under a half-a-day contract, there will be a 50 per cent reduction of his/her insured length of service, which is recognized and hence, this worker will accumulate less retirement points. This means that some of the bad-faith employers will seek other options for bypassing the insurance thresholds, namely civil (service) contracts or relocation of the employees to a position with a lower pay.

Employers in general welcome the government measures for curbing gray economy and for the mandatory registration of labor contracts, but they are of the opinion that the compliance of the requirements as they have been adopted will result

in additional and unnecessary company costs, and this will deteriorate the business conditions in the country. The MLSP plans to introduce also another measure in the beginning of 2003. **A provision, which is about to be put forward for consideration prior to the second reading of the new Social Security Code, stipulates that employers, who conceal, avoid or fail to pay social security contributions will be put in prison.** This provision will be laid down in the transitional and final provisions of the Social Security Code, on the basis of which later on amendments will be made to the Penal Code as well. The justification is that by committing the above-mentioned acts the employers violate the constitutional right of employees to be insured after they have done their job. The truth is that the government aims at implementation of higher revenue, which is planned to come to the social security budget from social security contributions, and at resolving the problem with the Pensions Fund deficit. Pursuant to the Mandatory Social Security Code a person, who violates the Code provisions or fails to fulfill a binding instruction by a control body, will be imposed a fine of BGN from 50 to 1,000, unless a more severe sanction is provided for. In case of repeated violation the fine will be from BGN 500 to BGN 2,000. Obviously such measures are not efficient enough, given the fact that the liabilities to the NSSI are constantly increasing. The intention is the new measure to make employers in breach to pay their liabilities.

The new Social Security Code is expected to repeal the requirements to the occupational pension funds to gather a minimum of 15,000 members in order to continue existing.

This will bring a final resolution to the problem with such funds, where over 150,000 individuals, working under conditions of 1st and 2nd labor category, pay for insurance for a second pension. In compliance with the currently applicable legislation, in case within two years after obtaining a license the three types of insurance funds fail to gather the required minimum number of insured individuals, they will not be allowed to continue existing. The 2-year term for the eight licensed occupational pension funds expired at the end of November, however four of them had not yet managed to meet the above requirement. These four occupational funds are: Rodina, ING, LUKoil Garant and Nuton Sila. The occupational fund of the Bulgarian Pension Insurance Company also has less than 15,000 insured, but due to its merger with Doverie Occupational Pension Insurance Company this is no longer a problem. It was expected that in the waiting period until the second reading of the new social code, an amendment to the Mandatory Social Security Code would be applicable, which provided for extension of the deadline for one more year. That amendment got to first reading only, too. Thus a situation occurred, which according to representatives of the Pension Funds was a legal paradox. The Mandatory Social Security Code does not provide for any measures, which the State Insurance Supervision Agency (SISA) should take in such situations. Ridiculous is the situation where, if the license of such companies is withdrawn, they would not be permitted

to manage the two other funds (universal and voluntary), either, while such a measure is unthinkable, because it would undermine the faith in the supplementary pension insurance reform as a whole.

One cause of the problem is the change in the criteria for labor categorization. Thus the number of people, working under 1st and 2nd category of labor decreased from 300 – 400,000 people to 150,000 at present. Another cause is the lack of a general procedure for changing the membership, that is, the Funds, which do not meet the criteria, to be given the opportunity to manage to meet the criteria through transferring insured persons from other pension funds.

In the draft of the new social code there was a provision stating that **the commissioned officers** should have supplementary pension insurance in a universal pension fund; this provision came as a big surprise to the pension funds, because it had not been discussed in the working group that had prepared the amendments to the social security legislation. According to data from the Funds the provision will refer to approximately 100,000 individuals, most of which (about 70,000) had voluntarily chosen a Fund, where to pay insurance for a second pension. According to the companies the justification of such an amendment sounds unreliable: excluding the commissioned officers from the pension insurance in universal pension funds is required because their personal information is classified. In practice this means more money to the budget of the State Social Security system and a potential for current pension benefits payment. There are grounds for the dissatisfaction of the private pension companies because they will not only lose the money, but also they will not be able to cover the costs they have incurred for attracting the military for a second pension insurance. It is obvious that the purpose is special regimes to be established for certain categories of citizens, which means that insured persons are not treated equally. Ultimately, in compliance with the adopted 2003 Social Security Budget Act the social security contributions for this category of individuals will still be paid both to the Funds, and to a universal pension fund for supplementary mandatory pension insurance.

The introduction of minimum insurance thresholds by sectors and professions, as well as the labor contracts mandatory registration with the NSSI starting 2003 was one of the most largely discussed topics in the public space at the end of 2002. Whether these two administrative measures taken by the MLSP will prove out to be sufficiently efficient for raising the collection rate of the social security contributions and reducing the grey economy share, is a matter of time to show. The government's good intentions to guarantee the security of the working individuals will not be sufficient, because ultimately everything depends on the working individuals' attitudes. Most of them prefer to work and be insured on the basis of the amount suggested by the employer, rather than being out of job.

Supplementary Pension Insurance

According to data by the State Insurance Supervision Agency (SISA), as of 30 November 2002 Complementary Pension Funds covered a total of 1 748 861 insured persons. Voluntary Pension Funds covered 478 521 insured persons, and Universal Pension Funds – 154 846 insured persons. As of 30 November 2002 net assets of SPFs amounted to a total of BGN 310 341 thousand, including 58 per cent in VPFs, 30% in Occupational Pension Funds, and 12 per cent in UPFs. As at end of September 2002 assets of pension funds amounted to BGN 279 200 thousand, which means that in the two months that followed assets of pension funds increased by 11 per cent. As of 30 November 2002 the tendency to invest assets of pension funds mainly in Government-issued or Government-guaranteed securities, in bank deposits and mortgage bonds was preserved.

Universal Pension Funds

According to data by SISA, as of 30 November 2002 UPFs covered 1 115 494 insured persons. Döner attracted the highest number of insured persons (422 157 people or 38 per cent), followed by Allianz Bulgaria (231 102 people or 21 per cent) and Saglasie (141 678 people or 13 per cent). As of 30 November 2002 net assets accumulated in UPFs amounted to BGN 37 193 thousand. Döner accumulated the highest amount of assets (BGN 13 454 thousand or 36 per cent), followed by Allianz Bulgaria (BGN 8 452 thousand or 23 per cent) and Saglasie (BGN 4 650 thousand or 13 per cent). As of 30 November 2002, 79.2 of investments by UPFs were made in Government-issued or Government-guaranteed securities, 16 per cent - in bank deposits in the country, 3.96 per cent - in securities traded at the regulated security markets, 0.54 per cent - in real estate, and 0.30 per cent - in municipal bonds. According to data by SISA, assets in UPFs are not invested abroad yet.

Occupational Pension Funds

According to data by SISA, as of 30 November OPFs covered 154 846 people, including 138 193 people, or 89 per cent in occupational class II, and 16 653 people, or 11 per cent in occupational class I. Döner attracted the highest number of people (54 987 people or 36 per cent), followed by Allianz Bulgaria (34 587 people or 22 per cent) and Saglasie (29 319 people or 19 per cent). As of 30 November 2002 net assets accumulated in OPFs amounted to BGN 91 834 thousand. Döner accumulated the highest amount of assets (BGN 34 217 thousand or 37 per cent), followed by Allianz Bulgaria (BGN 23 818 thousand or 26 per cent) and Saglasie (BGN 16 566 thousand or 18 per cent). As of 30 November 2002, 70.68 per cents of investments by OPFs were made in Government-issued or Government-guaranteed securities, 24.06 per cents - in bank deposits in the country, 4.37 per cent - in securities

traded at the regulated security markets, 0.68 per cent - in real estate, and 0.21 per cent in municipal bonds. According to data by SISA, assets in OPFs are not invested abroad yet, just like assets in UPFs.

Supplementary Voluntary Pension Insurance

According to data by SISA, as of 30 November 2002 Voluntary Pension Funds covered 478 521 insured persons. Allianz Bulgaria attracted the highest number of insured persons (247 920 people or 52 per cent), followed by Doverie (88 164 people or 18 per cent) and BPIC (34 344 people or 7.2 per cent). As of 30 November 2002, net assets accumulated in VPFs amounted to BGN 181 314 thousand. Allianz Bulgaria accumulated the highest amount of assets (BGN 97 718 thousand or 54 per cent), followed by Doverie (BGN 28 172 thousand or 16 per cent) and Lukoil Garant - Bulgaria (BGN 14 926 thousand or 8.2 per cent). As of 30 November 2002, 57.44 per cent of investments by VPFs were made in Government-issued or Government-guaranteed securities, 36.10 per cent - in bank deposits and mortgage bonds, 4.34 per cent - in real estate, 1.34 per cent - in securities traded at the regulated security markets, 0.55 per cent - in municipal bonds, and 0.23 per cent - in other types of investments. According to data by SISA, as of 30 November 2002 VPFs do not have investments abroad.

Employment, Unemployment and Labor Market Policy

The trend of decrease in the number of individuals registered with the Labor Offices continued in the fourth quarter of 2002, too. That number is decreasing every next month, although this is not quite clearly perceived yet. In November for the first time the rate of unemployment exceeded the 17 per cent level of the economically active population. The trend of decrease in the number of unemployed is in line with the processes of employment increase, established through the regular workforce surveys conducted by the NSI.

The reasons for the decrease are to be found in the devising and implementation by the MLSP of measures for subsidized employment, as well as in the less strongly manifested negative effects from the economy restructuring and the liquidation of companies operating at a loss.

At the end of the year the first assessment and analyses were made regarding the results of the pilot phase of **the program From Social Assistance to Providing Employment**. This is an absolutely required prerequisite for the program extension in the next year. All municipalities involved in the pilot phase assess the program as useful and well timed, and also 90 per cent of their population approve of the idea job opportunities to be offered instead of social assistance.

The latest amendments to the Employment Enhancement Act provide for the program From Social Assistance to Providing

Employment to be implemented as a standing measure. The average annual number of individuals employed under the program will be 100,000 people, and the 2003 state budget has BGN 217 million allocated for this purpose. The program will cover all municipalities in Bulgaria, as well as ministries and agencies. Employers' co-financing under the program will amount to BGN 60 million. A definitely positive aspect of the program implementation, which has to be highlighted, is the incorporation of two new components: literacy and qualification training of the persons employed under the program.

The program development and implementation is a good example of partnership of the Ministry of Labor and Social Policy, local governments and employers, aimed at resolving the employment issues. All these partners are directly committed to the success of the measures against unemployment and poverty, an extremely important aspect being to actively involve the municipalities and build their capacity to put such initiatives into practice. Again the same aim is pursued by the projects for generating social capital in municipalities with high unemployment rates. These envisage rendering support to local initiatives for opening new jobs and starting own businesses in the districts of Silistra, Razgrad, Shoumen, Dobrich, Varna and Targovishte. These projects are significant also as a preparation for the launch of activities under the Social Investment Fund.

The program Support in Retirement was launched on 1 November 2002 throughout Bulgaria. According to its objectives by the end of 2003 14,200 individuals will obtain jobs so as to be able to accumulate the length of service required for retirement. The program is quite well timed because every next year the requirement to the length of service for retirement is increasing by six months and this reduces still further the retirement opportunity for such people.

Another employment program of the Ministry of Labor and Social Policy, titled Personal Assistant, was launched in the fourth quarter of 2002. It will give opportunity to people, who are taking care of an ill elderly person or a child with impairment, to be hired under a labor contract. According to preliminary estimates by the end of 2002 approximately 1,200 people were going to be involved in the above program and receive a minimum salary and social security. The estimates for 2003 are that approximately 10,000 individuals will be included in the program. The positive impacts of the program implementation may be seen as multifold, namely: generation of employment, recognition of the effort and care for people with disease as a regular employment, more human treatment of those in need of specialized care, etc.

Contribution, although insufficient, for the reduction of unemployment comes also from the **micro-credits program titled Micro-credits Guarantee Fund**. The funds planned for 2002 were BGN 20 million, and only about BGN 14 million

were used, which is an indication of insufficient administrative capacity. Approval was granted to more than 1,400 projects, which provide over 3,000 new jobs. The 2003 budget has BGN 13 million allocated for micro-credits, which means that the program implementation will continue at a limited scale. According to the agreement with the partner banks, the intention is an alleviated credit collateral regime to be introduced for long-term unemployed individuals, young people of age up to 29 years and people with disabilities. The applicants for micro-credits will receive also business consulting services, which will be delivered by the labor offices experts.

As a means for alleviating the pressure on the local labor markets the MLSP is working upon workforce exchange agreements with a number of West European countries. The significance of such agreements is to be found also in the aspect of restricting illegal emigration in the period preceding Bulgaria's accession with the European Union.

Income and Living Standards

The last three months of 2002 confirmed the trend of nominal and real increase of the population income according to the household budgets statistics. Despite the positive developments in the natural consumption of some basic foodstuffs, such as meat, dairy products, fruit and vegetables, the structure of consumption of Bulgarian households compared with the same period of 2001 generally does not show any increase in the living standards.

October 2002 marked the beginning of a positive trend of increased "consumer trust", the relevant indicator being 8.0 points higher than its July level. The consumers' pessimism is decreasing with regards to all questions in the questionnaire. **The opinions about the changes in the households' financial situation are more favorable.** Compared with July, in October the balance of opinions regarding the question, which assesses the current condition of households budgets has improved by 5.4 points. Further on, the relative share of the people, who "accumulate higher debt" has decreased by 5.2 points, and the share of those "who make both ends meet" has increased by 2.5 points. An improvement in the family finances has been established with all categories of individuals, with the exception of those who are employed part-time.

It is of significant importance to point out that consumers' **expectations regarding consumer prices and unemployment in the next 12 months are definitely optimistic.** Consumers' expectations regarding the possibility for saving and the intention of making purchases are more favorable by 5.6 points and 3.8 points increase in the balances respectively.

Social Assistance

In the fourth quarter of 2002 a statutory amendment of significant importance was made to the current government's social policy. We mean the **application of a differentiated approach in the social assistance**, thus achieving more efficient resources allocation to those who are most in need (such as lonely elderly people of age above 75 years, people with disabilities, single parents). Through the amendment to the Regulation for the Application of the Social Assistance Act, which introduces the application of differentiated and increased coefficients, in 2003 more than 100,000 individuals in disadvantaged social position will be receiving larger social benefits. The unemployed persons, who are paid social benefits, will have also further opportunities provided that they get involved in the program for giving and cultivation of land from the state and municipal land fund, where the revenues from the activities will not be taken into account when determining those individuals' entitlement to social assistance during the first year.

For the first time since 1999 the year was completed with no state liabilities to the municipalities for the payment of social benefits. In reality this means that all municipalities in Bulgaria will start the year 2003 with no deficit in these costs.

Social Partnership

The past year will be remembered also with the **amendments to the Labor Code**, which refer to the functions of the National Council for Tripartite Cooperation, and more generally for the social dialogue in Bulgaria in determining the social policy. Previously the government was obliged to coordinate with the social partners its position on all social policy matters. From now on this obligation will be valid only regarding matters of social security and labor rights. Naturally enough, employers and trade unions do not welcome this (as perceived by them) restriction of the social dialogue, but as a matter of fact only time will show how benevolent is the approach of all concerned participants in it: the government and the social partners.

The last three months of the year passed **without any substantial social tension and serious industrial conflicts.**

Discussions in the field of healthcare in the last quarter of 2002 were focused on the National Health Insurance Fund 2003 Budget Act, the amendments to the Health Insurance Act and the Human Medications and Pharmacies Act. The end of 2002 did not face the signing of the National Framework Agreement for the next year. The negotiations among the National Health Insurance Fund (NHIF), the Bulgarian Medical Association (BMA) and the Bulgarian Dentists Union (BDU) regarding prices and number of activities, to which the patients will be entitled and for which the NHIF will pay from its budget, are expected to start after the promulgation in the Official Gazette of Ordinance No. 27 on Determining the Main Package of Health Activities backed-up by the NHIF budget, and Ordinance No. 26 stipulating the list of diseases for the home treatment of which the NHIF will pay for the medications fully, or partially.

With the latest amendments to the Health Insurance Act the Government actually secured its right to make decisions and give instructions, while the NHIF's operational management must simply execute them. The Government's quota in the NHIF Representatives' Assembly has been increased to 18 people, while the employers, insured individuals and municipalities have only 6 representatives each. Prior to the amendments to the Health Insurance Act the Government, the employers and the insured individuals used to have an equal number of representatives each, namely 18 each, which was a precondition for fair decision-making regarding the NHIF. Moreover, the concluding of transactions and the cash flows operation has been transferred as an obligation and responsibility completely to the Managing Board for the future, and not to the Executive Director – this fact predetermines the key role of the state. The large balance to be carried forward, namely BGN 800 million, that has been accrued over the years from citizens' health insurance contributions continues to be kept frozen at the Bulgarian National Bank and to support the fiscal reserve of the country, instead of being used to the right purpose in compliance with the law provisions. The NHIF, however, has also another annual reserve of funds, designed for operational needs. In 2003 this reserve was increased by 10 percent with the proceeds from health insurance contributions collected through the year and it amounts to over BGN 73 million. The intention is that most of it be spent on medications because the funds available for medications were reduced when the NHIF budget was adopted. The NHIF in its draft-budget suggested BGN 201 million for medications; however, the Parliament reduced this amount to approximately BGN 163 million. The justification for this reduction has to do with the increased amount of the reserve, which can be operated more freely.

Unlike previous years, for the year 2003 it was decided that NHIF expenditure items be fixed and no transfer of funds "for filling gaps" be allowed in the cases where shortages occur. Besides using funds from the reserve, deficit can be covered also through transfer of funds from capital costs. The

purpose is to establish a better NHIF funds management that will guarantee efficient usage of the insured individuals' health insurance contributions.

According to data from the NSSI the collection rate of health insurance contributions from employers and self-insured persons is relatively high. Therefore, no increase of the health insurance contributions rates is planned by 2005. **In compliance with the NHIF Budget Act the health insurance contributions rate for 2003 will amount again to 6 percent of the income for insurance purposes and the ratio of allocation of the health insurance burden between employers and insured will be maintained at 75:25.** The expert opinion is that a better management of the health care funds will be achieved if the funds come from one and the same source. At present a part of the funds for hospitals come from the NHIF, another part comes from the budget of the Ministry of Health, while municipalities finance the municipal hospitals. In this way the funds for health care are not utilized efficiently, there is lack of uniform criteria, and the responsibility and control are not clear-cut enough. With a view to better management of the health care funds it is planned that by 2005 the NHIF will undertake completely the payment for in-patient care as far as medical care is concerned, while the capital costs will remain the owner's responsibility.

Although the two private health insurance companies Doverie and Zakrila have been licensed with a capital of BGN 2 million, in compliance with the **amendments to the Health Insurance Act that the minimum capital of a health insurance company at the time of filing an application for a license is currently BGN 500,000, the company being obliged to raise its capital up to BGN 2 million within three years after it is granted a license.** The purpose is the private health care services market to be entered by more private health insurance companies in order to foster the competition in this health care services market.

According to the NHIF 2003 Budget Act the funds allocated for health insurance benefits amount to approximately BGN 627 million. In comparison, in 2002 that amount was BGN 487 million. Every year the major problem is related to medications. In 2002 expenditures for medications reached BGN 240 million. This is the reason why the NHIF offers stricter financial control mechanisms, which will guarantee the efficient use of the funds allocated for medications. Such a mechanism is adherence to the so-called "reference value principle". What it meant is providing an incentive for using medications with the lowest treatment course price within a certain group of medications, which is paid for by the citizens. On the other hand, there is a strive for determining a threshold price for the treatment of each disease, and that price to be paid by the NHIF. The foregoing is expected to be achieved by means of planning the costs in compliance with specified medical standards and requirements. The NHIF expects from these two mechanisms

to reduce the over-prescribing of medications, thus resulting in lower expenditures for medications. It is expected that in the beginning of 2003 the NHIF and the BMA will agree upon the conditions in the new health care agreement for 2003, which should ensure better quality and coverage of health care for the population. The limits on specialized doctor examination referrals and for laboratory testing are expected to be canceled in the new health agreement for 2003 because as practice shows such referrals limits are exhausted as early as in the first days of each month.

The budget for subsidies to state hospitals for 2003 is BGN 220-230 million, and the NHIF's funds for in-patient medical care amount to BGN 200 million. For payment of the treatment along clinical paths from 2003 on, the NHIF will have available BGN 200 million, compared to BGN 100 million for 2002.

Fostering the efficiency and effectiveness of in-patient care observing the requirements to accessibility, timeliness, adequacy and quality is the objective of the **Strategy for Restructuring of In-patient Care in Bulgaria**, which the government adopted in mid-November. **An Action Plan accompanying the Strategy** has been adopted as well and it covers the period until 2007. The main objective of this document is to make hospital care, the structure and number of health care establishments more rationally organized, and to strike a balance between the needs of hospital care and the required resources. The document envisages also the development of an investment strategy and investment program in health care. These will refer to the planning of funds for replacement of the medical tools and equipment with new ones, and will regulate the obligations of the government, the local governments and the health care establishments. The expectation is that the sector restructuring will ensure congruence between the health care needs of the population and the access to qualified medical care; improvement of the facilities and equipment of the health care establishments; optimal management of the financial resources and strict costs control, as well as improvement of the quality of services.

In November the government allocated BGN 55 million additionally to the 2002 budget of the Ministry of Health for settling the hospitals' liabilities; the aforementioned amount was accrued from budget savings. The expectation was that with this subsidy the hospitals would settle completely their liabilities, and two thirds of the hospitals would start 2003 free of liabilities in 2003.

By Decree No. 296 of the Council of Ministers for granting additional funds under the budget of the Ministry of Health the Council of Ministers stipulated that the Minister of Finance should submit from the 2002 State Budget additional funds under the Ministry of Health budget amounting to up to BGN 35,600,000. These funds were aimed for settling the liabilities

of health care establishments and the Ministry of Health for medications and medical consumables.

In the last quarter of 2002 the Minister of Health also approved, by virtue of two ordinances, the main package of health care activities, which is backed up by the NHIF budget, as well as the list of diseases for the home treatment of which the NHIF will be paying for the medications either completely, or partially. Ordinance No. 27 specifies the main packages of paramedical and specialized out-patient health care, activities in dentistry and in-patient care. For the first time the main package of activities in dentistry envisages the opportunity of treatment of citizens of the age up to 18 who are accommodated in homes for medical-social care of children, homes for upbringing and education of children deprived of parent care, and homes for mentally retarded young people and people with physical disabilities, as well as specialized schools. For pregnant women a one-time detailed examination is ensured for taking their dental status. The number of clinical paths has been increased by another 41.

Ordinance No. 26 gives the list of diseases for the home treatment of which the NHIF will pay for the medications either completely, or partially. The methods of reimbursement will be discussed in early 2003 with determining the parameters of the National Framework Agreement for the next year.

By adopting the Act on Amendments to the Human Medicine Drugs and Pharmacies Act at the end of December 2002 the Members of the Parliament introduced in the Bulgarian legislation data exclusivity to become applicable from the beginning of the next year; data exclusivity will have direct impact on the pharmaceutical companies. Directive 83 of the EU provides protection for 6 years of the medical dossier information of any drug in the cases of toxicological, pharmacological and clinical research on the product. The use of such data will be allowed only with manufacturer's permission. Data exclusivity is complied with by all EU Member States and is aimed at protecting the large pharmaceutical companies, which spend millions of dollars on medications development. It is different from the introduced patent protection of medications, which is for a 20-year term and protect the intellectual property rights of companies developing new medications.

A large public forum in the last quarter of 2002 united the efforts of the government and civil organizations in the implementation of environmental policy. In the beginning of October a **national eco-forum-expo was held titled Ecotourism, Mountains and Protected Areas – Partners for Prosperity**. This forum, which constituted Bulgaria's participation in the International Ecotourism Year (under the auspices of the UN Environment Program and the World Tourism Organization) initiated a discussion on the possibilities for achieving economic growth based on reasonable use of protected areas, development of ecotourism under market economy conditions, funding the tourist environmental activities, and the prospects of establishing competitive tourism clusters in Bulgaria. It can be perceived as a model of implementation of sustainable development objectives.

A presentation was made at the Forum of the first working version of the National Strategy for Ecotourism Development in Bulgaria – a document prepared under the Preserving the Biological Diversity and Economic Growth Project and uniting the efforts of experts of ministries, national and regional tourist associations, information centers and non-government organizations in the field of nature protection and regional development. In an Agreement signed at the Forum the three ministries (the Ministry of Economy, the Ministry of Regional Development and Public Works, and the Ministry of Environment and Water) came to an agreement to set up and institutionalize a joint working group for the completion in 2003 of the **National Strategy for Ecotourism Development in Bulgaria**.

Significant role in the implementation of environment policy priorities was assigned to local governments through the 2003 budget which was approved in December 2002. Developed on the basis of the program budgeting principle, this budget envisages BGN 173.7 million general environmental expenditures for 2003, 87 percent of which are allocated for funding municipal programs and projects. Together with the funds under European programs, the co-financing from the National Fund at the Ministry of Finance, the revenue from the State Agency for Management of the Environmental Protection Activities, and the targeted subsidies from the state budget to municipalities will allow for the implementation of large capital investments projects in two priority areas – solid waste management and water management.

Several environmental projects, which received funding form international organizations, deserve to be highlighted when speaking of the last quarter of 2002. Official launch was made of six investment infrastructure projects in Bulgaria approved under ISPA, namely:

- Collection and Treatment of Waste Water from Bourgas City, Meden Roudnik housing estate
- Collection and Treatment of Waste Water from Targovishte City

- Collection and Treatment of Waste Water from Sevlievo City
- Collection and Treatment of Waste Water from Lovech City
- Collection and Treatment of Waste Water from Montana City
- Collection and Treatment of Waste Water from Popovo City

The projects amount to a total of over EURO 87 million, of which EURO 65 million are grants. The financing conditions envisage international financial institutions to be attracted as co-financing organizations for the implementation of projects in the future. For all projects in 2002 the maximum percentage of grants allowed in compliance with the ISPA rules was allocated – 75 percent of the total investment value of each project. The national co-financing for implementation of projects that have obtained financial support form the EU, is ensured from the consolidated National Budget, and the funds allocated are managed by the National Fund at the Ministry of Finance.

The US Agency for International Development supported a project for the establishment of a specialized Parks and Protected Areas Fund. This Fund will raise funds mostly from foreign donor programs. The Ministry of Environment and Water has submitted to the World Bank a USD 2 million proposal for getting the Fund started.

The agreement signed between the Republic of Bulgaria and the Prototype Carbon Fund at the International Bank for Reconstruction and Development is expected to be ratified by the Parliament in the beginning of next year. Two projects will be launched as a result of the above-mentioned agreement, namely: a project for efficient use of biomass as a fuel at Svilozha AD (Svilozha Rayon Plant), and a project for improving the energy efficiency of Sofia and Pernik power plants.

In October a public presentation was made to raise public awareness of the activities under the project Wetlands Restoration and Pollution Reduction in the protected area Kalimok/Brushlen; the funding for this project was approved by the World Bank in June 2002. The project funding comes from grants under the Trust Fund of the Global Environment Fund (GEF) and amounts to USD 7.5 million, the co-financing from the Bulgarian party amounts to USD 3.05 million, and the funding from other foreign donors amounts to USD 2.73 million.

The project objective is to assist in the rehabilitation of biodiversity in degraded habitats and in mastering sustainable natural-resources management practices by the local communities and authorities in the Persina natural reserve and the Kalimok/Brushlen protected area, to be exercised by actions aimed at wet land rehabilitation back to their optimal status in this region.

Table 11. Monitoring of Negotiations for Bulgaria's Accession to EU

Chapter	Status (31 st December, 2002)
1 Free Movement of Goods	Temporary closed
2 Free Movement of Persons	Temporary closed
3 Freedom to Provide Services	Temporary closed
4 Free Movement of Capital	Temporary closed
5 Company Law	Temporary closed
6 Competition Policy	Open
7 Agriculture	Open
8 Fishery	Temporary closed
9 Transport Policy	Open
10 Tax Policy	Temporary closed
11 Economic and Monetary Union	Temporary closed
12 Statistics	Temporary closed
13 Social Policy	Temporary closed
14 Energy	Temporary closed
15 Industrial Policy	Temporary closed
16 Small and Medium-Sized Enterprises	Temporary closed
17 Science and Research	Temporary closed
18 Education and Training	Temporary closed
19 Telecommunications	Temporary closed
20 Culture and Audiovision	Temporary closed
21 Regional Policy	Open
22 Environment	Open
23 Consumer Protection	Temporary closed
24 Justice and Home Affairs	Open
25 Customs Union	Temporary closed
26 Foreign Relations	Temporary closed
27 Common Foreign and Security Policy	Temporary closed
28 Fiscal Control	Temporary closed
29 Fiscal and Budgetary Issues	Open
30 Institutions	Temporary closed
Total chapters closed	23

The period October - December 2002 is characterized by important to Bulgaria decisions and events. The Seventh Session of the Conference on Negotiations for Bulgaria's Accession to the European Union was held in Brussels on 1 October, 2002 at minister-level. **The Conference concluded that the achieved progress in the field of fiscal control enables to close negotiations on Chapter 28: Fiscal Control, and confirmed the agreements reached at deputy-level on Chapter 25: Customs Union.** The Danish minister of foreign affairs stated that the road map for Bulgaria adopted by the European Council in Copenhagen will allow to preserve the pace of negotiations. A special package to accelerate Bulgaria's membership to the European Union is envisaged for the purpose. Thus, nearly three months before the Copenhagen Summit it became clear that the European Commission will recommend full support for the country and the equal treatment principle will be a major priority in its recommendations.

The 2002 Regular Report of the Commission on the Progress of Bulgaria was published a few days later, on 9 October 2002. **It is stated for the first time that Bulgaria is a functioning market economy. The 2001 assessment**

classified Bulgaria as a country close to the functioning market economy.

Major conclusions for Bulgaria set forth in the Commission's Strategic Document on Enlargement include:

Political criteria:

- considerable progress in the judicial reform;
- positive anti-corruption development;
- progress in the administrative reform;
- permanent respect of human rights and freedoms;
- reducing discrimination on account of individual's sexual orientation;
- poor living conditions in mental homes;
- a need to increase efforts for reform of the child care system;
- improving the living conditions of prisoners;
- little has been done in respect of Bulgaria's Roma population;
- a need to fight corruption.

Economic criteria:

- Bulgaria is a functioning market economy;
- Bulgaria has achieved a high level of macroeconomic stability; market mechanisms function properly;
- considerable progress of structural reform, financial sector restructuring, and privatization;
- a need for further efforts to improve market flexibility;
- a need to simplify banking procedures;
- the level of financial intermediation remains low;
- land market differences are not overcome yet.

Implementation of the Acquis Communautaire:

- Bulgaria has achieved acceptable level of harmonization with European legislation;
- national administrative capacities have developed, but there is a need for further efforts in this field;
- there is a need for continuous efforts to develop administrative and judicial capacities to adopt and implement European legislation;
- to become a part of the internal market, Bulgaria has to develop its capacities in fields such as agriculture, environment, and regional policy;
- there is a need to build administrative mechanisms with a view to ensure sustainable management of European funds;
- improving veterinary control and hygiene standards;
- there is a need to enhance the protection of intellectual and industrial property rights.

As early as 1997 the European Commission concluded that Bulgaria fulfilled the political criteria. Ever since the country has been making considerable progress, consolidating and enhancing the stability of its institutions, thereby guaranteeing democracy, rule of law, respect and protection of human and

minority rights. This trend was also confirmed in 2002. Bulgaria continues to fulfill the Copenhagen political criteria. The progress in economic development and administrative reform is positive. However, the above said indicates a need of further efforts to approximate Bulgarian to European legislation, to implement European standards, anti-corruption measures, to improve financial services and banking procedures, the management and utilization of European funds.

At a meeting in Luxembourg (on 22 October 2002) the foreign ministers of the Member States adopted a decision that Bulgaria and Romania would not take part in the 2004 European parliamentary elections and would lose their places set forth in the Nice Agreement. According to the 2000 Nice Agreement, the deputy quotas of all 12 European Parliament member-countries were determined according to the population of each country. Bulgaria got 17 places and Romania - 33. These two deputy quotas will be now distributed among the ten countries of the first wave.

On 29 October 2002 the European Commission signed with the candidate countries agreements for association to the Sixth Framework Program for research, technological development and demonstrations (2003-2006). The total program budget amounts to EUR 17.5 billion. All 13 candidate countries will sign a Memorandum with the European Commission and will specify their role and capacities to participate in the Sixth Framework Program. According to the Commission's decision, with regard to the Sixth Framework Program candidate countries will have the same rights and obligations as the Member States, which means that this will be the first area where enlargement will become a fact. Seven candidate countries (Bulgaria, the Czech Republic, Hungary, Latvia, Romania, Slovakia, and Slovenia) have stated their interest to get associated to the EurAtom Framework Program (2003-2006) for nuclear research.

With the temporary closing of Chapter 14: Energy Sector (18 November 2002) in accordance with the 1999 Memorandum, the Decision of the Council of Ministers of September 2002, and the Decision of the National Assembly of October 2002, the pace of the negotiations for accession was not preserved. This happened at the Eighth Session of the Conference on Bulgaria's Accession to the European Union held at minister-level.

The final part of the negotiations continued for more than 12 months. The Bulgarian side negotiated the conditions for integration of the Bulgarian energy market into the internal energy market of the European Union. In the course of negotiations special attention was devoted to building a national crude oil reserve in accordance with the requirements of EU general legislation. Bulgaria managed to negotiate a 6-year transitional period starting from the accession date - 1 January 2007, to complete the reserve.

The two sides devoted special attention to the nuclear power sector where Bulgaria insists on equal treatment with the other candidate countries. The position of firm rejection of

the "nuclear energy sector" expressed by the governments of some member-states is well known, and EU decisions are only adopted with the agreement of all 15 Member States.

The fifteen Member States agreed to a peer review to analyze the safety level of the two small units. This peer review was requested by the Bulgarian side in fulfillment of CoM's position and Bulgarian Parliament's decision.

November was the month of another event of importance to Bulgaria. The Prague Summit (21 November 2002). **Bulgaria received official invitation for NATO membership.**

The European Council in Copenhagen (12-13 December 2002) adopted other important to Bulgaria decisions. **Bulgaria and Romania will become EU members in 2007, provided that they continue their progress in fulfilling membership criteria.** The Danish Presidency wanted to secure EU enlargement after 2004, when the union will comprise 25 states, by engaging the countries of the first wave with the membership of Bulgaria, Romania, and Turkey.

The road maps presented by the European Commission set clear goals for Bulgaria and Romania and enable each country to determine its own pace in the process of accession. It is essential for the two countries to make use of this opportunity by accelerating their preparation, including in the fulfillment and implementation of the commitments undertaken in the negotiations for accession.

The Conclusions of the European Council in Copenhagen state that "finalization of the negotiations for accession with ten candidate countries accelerates the prospects for accession of Bulgaria and Romania as part of the same irreversible enlargement process".

In the middle of November 2002 the European Commission announced a plan to increase pre-accession support. In 2004 Bulgaria and Romania will get an increase of 20 per cent, in 2005 - 30 per cent, and in 2006 - 40 per cent. The total contracted amount from pre-accession funds for Bulgaria is EUR 1 500 000 000 for the period 2003-2006. The European Union offers EUR 40.4 billion for the ten new Member States for the period till 2006. After their accession to EU on 1 May 2004, the new members will have to make annual contributions to the Brussels budget, which amount to around EUR 15 billion for the period till the end of 2006.

The overall assessment of the negotiations for accession reveals that 15 years after the "Iron Curtain" was lifted the first large group of CEE countries (Cyprus, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia) will join the European Union. These ten states are expected to officially become members on 1 May 2004. At the Copenhagen meeting they closed all chapters for negotiation. Bulgaria has temporarily closed 23 chapters for negotiation, and Romania - 16 chapters.

A positive effect on the business conditions in the country is exerted by two extremely important circumstances, namely: the recognition given to Bulgaria for a functioning market economy and the road map for accession to the EU, and the invitation to NATO membership. These two events are of considerable importance although their effect on the economy is not a direct and immediate one. In any case, however, these raise better certainty and confidence among the potential partners and investors in the country. **The following should be added here: the Agreement with the IMF, and the Decision passed by the World Bank for granting the PAL loan** (in November last year the World Bank made a decision to grant the loan under the PAL program amounting to USD 150 million, which is a part of the WB's program for Bulgaria with a view to supporting its balance of payments). Indisputably, these are facts, which both in the short-term and long-term, will have a positive impact on the business climate in the country, too.

In October **the government announced a package of 9 legislative and structural measures for improvement of the business climate and enhancement of economic growth** ("The Vassilev Program"). These measures include: establishment of an investment fund with state participation; setting up of industrial zones; amendments to the Commercial Law in its section related to insolvency and liquidation; resolving the problem of companies' mutual indebtedness; capital markets development; establishing a real estate market index; removing and simplifying licensing, permission and registration regimes; fostering the role of the Bulgarian Export Insurance Agency; taxation and social measures.

Some of the measures are directly targeted at business climate improvement – alleviation of licensing regimes and amendments to the Commercial Code; others are aimed at attracting and enhancing foreign investments, and mostly "green" investments (the industrial zones).

The announced measures are assessed differently by business representatives and experts. Some of the measures are perceived in connection with problems that will arise in the course of their implementation – for example, the establishment of industrial zones may have controversial impact and may lead to problems in the negotiations with EU on the Competition Chapter. This is true also for the Venture Capital Fund where some negative consequences are possible, too, which necessitates the developing and applying of clear rules for financing, monitoring and paying back the investments in the Risk Fund.

Most of the announced measures are tied to changes in the regulations and adoption of new laws, which is time consuming and in reality many of these measures may be enforced only in the next year and later. However, those intentions may be estimated as positive ones, mostly as an expression of the

trend towards improvement of the business conditions in the country and stimulation of the growth.

Licensing Regimes

The licensing regimes reform is being carried out but at a slow pace. It started as early as 1999 and according to the new program it should take place in three stages. The first stage was completed to some extent in May when 74 regimes were repealed and another 120 regimes were eased. The second stage provides for improving the information exchange among all government structures related to the issuing and controlling of licenses. The objective of those proposals was saving time and resources when considering the applications for issuing of licenses. The implementation of that second stage, however, is lagging behind.

The third stage provides for adoption of **Law on the Statutory Acts and Administrative Proceedings Related to Economic Activities**. The draft law provides for all requirements for carrying out economic activities to be explicitly stipulated in the Law. It is expected that in this way the administration will be restricted in creating additional requirements and limitations for the business at their own discretion.

The Law will define three basic regimes - licensing, certifying and notifying. In this way the qualification of the regimes will be clearer and simpler.

Public Procurement

The special working group on the drafting of new amendments to the Public Procurement Act, constituted at the Council of Ministers, the Act being already amended in the spring, continued its work in the fourth quarter.

The amendments discussed are related to appealing of the procedures, relieving the terms of assigning public procurement orders by the utilities, looking for opportunities to introduce preferences for Bulgarian companies. It has been considered that Public Procurement Directorate at the Council of Ministers should retain only its administrative functions, and another arbitration institution should be established for hearing the appeals of discontented candidates for contractors that should adjudicate as a first instance and the court would be a second instance. The intention is the arguments to be settled exactly by this arbitration institution (the experience shows that in the countries where the arbitration institution is established only 1 or 2 out of 20 appeals reach the court). Another problem that has been considered: the Act as it stipulates that at least three tenderers should participate in an open procedure so that a company could be contracted, which creates difficulties with the less attractive public procurement orders. Therefore this provision should be amended, too.

Regulation of the Bankruptcy Procedures

The Ministry of Justice and the Ministry of Economy are drafting **a bill for amendments in the Commercial Code in its part about bankruptcy and liquidation**. The reform of the Trade Law in its part about bankruptcy and liquidation aims at the introduction of fast and efficient bankruptcy procedures. Logically the fast bankruptcy procedure is in the interest both of the debtors and creditors, as well as of the employers. In general terms those amendments mean drastic reduction of the procedures and shortening the terms for their execution, as well as improving the protection of the interests of good faith creditors.

The bill provides for amendments in the company law as well, giving more power to the shareholders and amending a number of details related to the holding of general assemblies and the majority required for adopting resolutions. A new chapter is added that regulates the procedures of merger, takeover, splitting, division, splitting to form a sole-proprietor company into sole proprietor company and others.

Judicial System

The Regular Report of the European Commission (EC) about the progress of Bulgaria presented in October points out that Bulgaria should exert further efforts for considerable strengthening of its judicial and law enforcement institutions. This is one of the areas where the country has been seriously criticized by a number of international institutions.

In September, however, the Supreme Court judges attacked at the Constitutional Court the amendments in the Judiciary Law proposed and adopted by the Parliament.

There were other serious concussions, scandals, arguments and contradictions in the judicial system during the fourth quarter which confirmed the necessity of radical reforms in this field. Reports of international institutions, including the EC report, World Bank, judicial reform index developed with the assistance of the American Bar Association (ABA) and others have been released in November, which gave a low rating of the Bulgarian judicial system and stated that it is badly governed, insufficiently financed, clumsy, etc. The criticism in the ABA report was especially strong. The document includes very radical evaluation that provoked strong response from representatives of the judiciary branch in Bulgaria. Nevertheless, the other institutions support some of the findings, too. The White Book of the Bulgarian Industrial Business Association (BIBA) also identifies the judicial system as the main problem that stands in the way of the business.

Other events that point to the necessity of changes are: revoking

the government decision for the privatization of "Bulgartabak Holding" JSC, the contradictions regarding the general prosecutor, the "BTC" SPJSC deal, the arguments around the budget. The problems that continue to create obstacles are: the clumsy procedure for investigating magistrates in breach because of their strengthened immunity, the lack of political impartiality of the Supreme Judiciary Council, the warring interests of the different sections of the judicial system and others.

The majority in the Parliament declared its willingness to continue with the reforms in the judicial system. A referendum was also proposed in December on the necessity of such changes.

Fight against Corruption

In October "Coalition 2000" presented its corruption index for the month, that measures public attitude to corruption practices. The assessment of corruption in Bulgaria is 6.7 per cent for October which is almost 8 points higher than May 2002. Tolerance to corruption has increased according to the survey. The EBRD annual report presented in November also contains findings that corruption has increased. That report proposes also a method for quantitative measurement of corruption: namely, what part of companies' incomes are spent for unofficial payments to civil servants, or "bribe tax". The average percentage of companies' incomes paid as a "bribe tax" in Bulgaria in 2002 is 1.9 per cent according to the bank team. Furthermore 33 per cent of the companies state that they had to give a bribe in 2002.

But at the same time the Report of the World Economic Forum, presented in November, too, states that the most positive and optimistic results that Bulgaria has achieved during the last year are related exactly to combating corruption - the country has moved up significantly in the first half of the group of countries with lower levels of corruption. It probably means that **it is hard to measure precisely corruption and the estimates are often contradictory. Nevertheless the problem is very serious and is a priority for all institutions in the country.**

The Commission for Combating Corruption established at the Parliament in September 2002 started its work but the coordination of the different groups participating in the process should be improved. Besides improving the legislation, the political will, the change in people's way of thinking and mentality is very important, too.

Administrative Reform and Support for the Business

In December the Government adopted a **Concept for Improving the One-Stop-Shop Service and "e-Government Strategy"**. The objective of such documents is to facilitate citizens, businesses and public administration, to reduce

the corruption sources and to save time and money. Those documents presume that all services will be provided through Internet. The Strategy envisages a minimum package of services provided through Internet to be introduced by 2005 - 12 services for the citizens and 8 services for the business. Especially for the business the relieves will be related to possibility for payment of taxes, duties and fees through Internet. Possibilities for sending documents through Internet is also envisaged. Pilot administrations have been identified that started the introduction of the One-Stop-Shop Service Model. The introduction of that model in Bulgaria is funded by United Kingdom. A package of legislative measures for the introduction of e-Government has been developed, too.

**ANNEX 1: NEWLY PASSED LEGISLATION
PROMULGATED IN THE FOURTH QUARTER OF 2002**

Title	Status	Official Gazette
Government debt ACT	New	NO. 93 OF 1.10.2002
TARIFF of Fees, To Be Collected Pursuant To the Tourism ACT	New	NO. 93 OF 1.10.2002
ORDINANCE on Licensing Tour-operator and Tourist Agency Activities	New	NO. 93 OF 1.10.2002
ORDINANCE on Categorization of Tourist Sites	New	NO. 95 OF 8.10.2002
ORDINANCE NO. 14 OF 2001 on the Conditions and Order for Extending Financial Grant for Investments in Farms under the Specialized EU Pre-accession Program for Development of Agriculture and Rural Areas in Bulgaria (SAPARD)	Amended	NO. 95 OF 8.10.2002
Insurance ACT	Amended	NO. 96 OF 11.10.2002
Farmers Support ACT	Amended	NO. 96 OF 11.10.2002
ORDINANCE on the Conditions and Order for Setting Current Market Prices of Agricultural Land	Amended	NO. 96 OF 11.10.2002
Privatization and Post-privatization Control ACT	Amended	NO. 96 OF 11.10.2002
ORDINANCE NO. 8 OF 3.10. 2002 on Duty-free Trade	New	NO. 96 OF 11.10.2002
ORDINANCE on Categorization of Agricultural Land in Case of Change of Its Intended Purpose	New	NO. 96 OF 11.10.2002
DECREE No. 65 of the Council of Ministers OF 1998 on Adoption of National Accounting Standards	Amended	NO. 97 OF 15.10. 2002
Environmental Protection ACT	New	NO. 91 OF 25.09.2002, AMENDED NO.98 OF 18.10.2002
Ownership and Use of Agricultural Land ACT	Amended	NO. 99 OF 22.10.2002
Civil Proceedings CODE	Amended	NO.105 OF 8.11.2002
Health Insurance ACT	Amended	NO. 107 OF 15.11.2002
National Revenue Agency ACT	New	NO. 112 OF 29.11.2002
ORDINANCE NO. 7 OF 1999 on the Large Exposures of Banks	Amended	NO. 113 OF 3.12.2002
Banking ACT	Amended	NO. 114 OF 6.12.2002
Value Added Tax ACT	Amended	NO. 117 OF 17.12 2002
ORDINANCE on Formation and Application of Heating Power Prices and Tariffs	Amended	NO. 117 OF 17.12 2002
ORDINANCE on Disclosure of Share Participation in a Public and Investment Company	Amended	NO. 117 OF 17.12 2002
ACT on Bank Deposit Insurance	Amended	NO. 118 OF 20.12 2002
Natural Persons' Income Taxation ACT	Amended	NO. 118 OF 20.12 2002
Excise Duty ACT	Amended	NO. 118 OF 20.12 2002
Social Assistance ACT	Amended	NO. 118 OF 20.12 2002
Local Fees and Taxes ACT	Amended	NO. 119 OF 27.12.2002
State Social Security 2003 Budget ACT	New	NO. 119 OF 27.12.2002
National Health Insurance Fund 2003 Budget ACT	New	NO. 119 OF 27.12.2002
Corporate Income Taxation ACT	Amended	NO. 119 OF 27.12.2002
ORDINANCE on the Order and Conditions for Public Procurement Relating to the Country's Defense and Security	New	NO. 119 OF 27.12.2002
ORDINANCE NO. 5 OF 12.12.2002 on the Order and Conditions for Acquisition, Payment and Trade in Government Securities	New	NO. 119 OF 27.12.2002
ORDINANCE NO. 15 OF 12.12.2002 on Control over Transactions with Dematerialized Government Securities	New	NO. 119 OF 27.12.2002
2003 State Budget of the Republic of Bulgaria ACT	New	NO. 120 OF 29.12.2002
ACT on Amendments to the Labor Code	Amended	NO. 120 OF 29.12.2002
ACT on Amendments to the Human Medications and Pharmacies ACT	Amended	NO. 120 OF 29.12.2002

A. REVIEW OF BULGARIA'S ECONOMY

The present review of Bulgaria's economy is an authentic expert product of the Center for Economic Development, which was made possible mostly owing to the long experience of the Center in the field of applied studies of the economic policy and economic development of the country.

The review of Bulgaria's economy in the fourth quarter of year 2002 contains detailed presentation of this past period, and assessment of the period and the trends after that. The review is explicitly focused on the fourth quarter of the year. Where necessary significant events, facts and data of the period prior to the quarter or after it have been highlighted. Where possible two main types of data comparisons have been made: against the respective period of year 2001 (or end of 2001), or against the preceding quarter (or its end). Again where possible, the dynamics within the fourth quarter *per se* has been traced, too. At many points also the trends for the near future have been outlined.

The structure of the presentation above follows two principles simultaneously. First, the strive is to give a more comprehensive presentation of the subject matter areas, with prioritizing the set of matters discussed. Secondly, the different topics and analyses reflect the experience and interests of the experts and of the Center for Economic Development as a whole.

The review of Bulgaria's economy in the fourth quarter of 2002 starts with the results from the business climate survey. The latest values of the Bulgarian business climate Estat index have been presented. The state and prospects of the business environment in our country have been analyzed based on the results from the survey. The business surveys of the National Statistical Institute (NSI) are presented immediately after that.

The overall economic dynamics in the fourth quarter of 2002 has been discussed against the background of the following basic categories: GDP, inflation rate and labor market. The fiscal review of the quarter starts with the execution of the budget. The fiscal review includes also the taxes, duties, external and internal debts topics. The privatization topic is followed by discussion on small and medium-sized enterprises. The foreign economic relations followed by foreign investments are presented in statistical terms by means of the balance of payments and in purely thematic relation. Then comes the review of a number of sectors of significant importance to the economic development of Bulgaria – energy, transport, high technologies, communication, tourism and agriculture. The financial sector is discussed by means of the capital market and the banking system. The wide topic of social policy and industrial relations encompasses the issues of social security,

employment and unemployment, labor market policy, incomes and living standards, social assistance and social partnership. The current problems in the healthcare reform have been discussed shortly. The environmental policy is considered simultaneously as a specific component of the economic policy and a factor for the economic environment. The specialized analysis of the process of Bulgaria's accession to the EU is underpinned by the understanding that in the course of these negotiations often the most determinative components of economic policy are defined. There exists a two-way interdependence between the competitiveness of the Bulgarian economy at macro- and company level, and the progress of the negotiations. That is why in the context of the review and analysis in general of the Bulgarian economy in the fourth quarter the choice was made to lay down the emphasis on the negotiations for EU membership as the most significant aspect of the European integration process, which encompasses the adaptation and application of *acquis*.

An integral part of the presentation is the enclosure with a list of the recently adopted or amended acts of high importance for the economic development of the country, published in the Official Gazette in the fourth quarter of 2002 (Annex 1).

This work was finally completed on 10 March, 2003.

B. SOURCES

Alongside with the conclusions from the large number of their own outputs and works, some of which are parts of specific research projects, the experts of the Center for Economic Development have used statistical and other input information and data from the following sources:

- National Assembly
- Council of Ministers
- Ministry of Agriculture and Forestry
- Ministry of Economy
- Ministry of Environment and Water
- Ministry of Finance
- Ministry of Labor and Social Policy
- Ministry of Regional Development and Public Works
- Ministry of Transport and Communication
- National Statistical Institute
- National Social Security Institute
- Employment Agency
- Agency for Small and Medium-size Enterprises
- Privatization Agency
- Bulgarian National Bank
- Bulgarian Stock Exchange – Sofia AD
- State Insurance Supervision Agency
- State Energy Regulatory Committee

- Delegation of the European Commission
- European Union
- International Oil Exchange, London
- EUROSTAT
- Official Gazette

The particular sources and publications are quoted at the respective places in the text.

C. THE ESTAT INDEX OF BUSINESS CLIMATE IN BULGARIA

The business climate survey is based on own original methodology, developed by a team of the Agency for Social and Marketing Surveys Estat and the Center for Economic Development. The more significant details are discussed below.

Methodology of the Sample

The survey was conducted between 6th and 10th January 2003 among the managers of 399 companies. The sample is a two-level panel one (at the first level the companies are divided into groups by regions, and at the second level – according to their economic sectors as per nomenclature A6 of the NSI), and it is grouped on the basis of the indices “number of employees” and “type of ownership”. The sample is representative at the level of going concerns.

Methodology of the Registration

The information has been collected using the method of an inquiry at the work place. The interviews were held with the owners of the companies included in the sample, or with persons authorized to make management decisions and to sign accounting statement documents (managers, chief accountants, commercial or marketing directors).

The questionnaire contains eight substance questions and three passport questions. The integrated index is comprised of three components. Questions from one to five included Component I – “General Condition of the Company”; question six – Component II – “Investment Attitudes and Company’s Strategies”; questions seven and eight - Component III – “Business Climate”.

General Outline of the Index Calculation

1. Preliminary Preparation

The preliminary preparation includes weighting the data

according to “economic sector” and “number of employees”, recoding and calculating values for the respective questions:

- Questions with one possible answer
The original scales are of Likert type with codes from 1 (the highest degree) to 5 (the lowest degree). Recoding is done in such a way that the scale to be from –2 (the lowest degree) to +2 (the highest degree).
- Multiple choice questions
These questions are recoded in advance in such a way that the possible answers are located symmetrically on both sides of the neutral point (the zero).

2. Calculation of the components

The index for each question (indicator) is calculated as an average weighted value.

Weights are assigned to each indicator within a component by means of expert evaluation. The value for each component (“General Condition of the Company”; “Investment Attitudes and Company’s Strategies”; “Business Climate”) is calculated as an average weighted value.

The first table above shows the values obtained for the three components and the integrated index.

3. Calculation of an integrated index

The integrated index is calculated as an average weighted value from the three components. The weight for each of the components is determined by means of expert evaluation.

The Estat index of the business climate assumes values from –100 to +100. The business climate condition is assessed according to the following scale, similar to the one used in the German IFO Business Climate Index:

-100 to –61	very bad
-60 to –21	bad
-20 to +20	average
+21 to +60	good
+61 to +100	very good

Interpretation

All components (with no exception), as well as the integrated index assume values within the interval [–100, +100]. The toolkit allows for determining also the direction of the index. The difference between the values of questions Q3 (assessment of the expected condition), Q2 (assessment of the condition at

METHODOLOGICAL NOTES

a certain moment) and Q1 (assessment of the condition during the preceding period) is taken as a criterion for determining the direction.

Beside everything said about the methodology here above, in many cases throughout the text additional methodological and other related notes and comments are given.

PART TWO

THE BULGARIAN ECONOMY IN 2002 (SUMMARY)

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The Bulgarian Economy in 2002 registers contradictory trends of development. On the one hand, good macroeconomic indicators are generally manifested in preserved fiscal stability and continued high GDP growth. On the other hand, indications of concern are registered at company level and in a number of sectors. Government's economic policy falls short of expectations. There is no substantial improvement of the business environment.

The Estat Index of business climate for 2002 remains within the neutral portion of the scale (varying from -0.998 for the first quarter to -2.55 for the last quarter of the year), which interprets the business environment as neither favorable, nor unfavorable. Nevertheless, the index registers a stable downward trend. Economic growth, taken on an annual basis, is expected to exceed the latest official estimates of a growth of 4.2 per cent. Early summarized data about the 2002 fiscal program, reveal that basic budgetary parameters have been fulfilled. Realized deficit is estimated at BGN 218.3 m., or 0.7 per cent of GDP, with planned deficit of BGN 257.3 m., or 0.8 per cent of GDP. In 2002 total amount of government and government guaranteed debt decreased by BGN 2 600 m., dropping down to BGN 18 180 m. at year end. Restructuring and privatization of the state sector continued in 2002, but the year was the worst for Bulgarian privatization since 1995. As of 31 December 2002, the number of privatization transactions concluded was only 275, according to data by PA; the annual plan is fulfilled at 41.4 per cent. Conditions for development of small and medium-sized enterprises did not register any material improvement in 2002. Total exports for 2002 (estimated at USD 5 578.1 m. and assessed by our team at USD 5 750 m.) exceed by nearly 12.5 per cent the 2001 amount (USD 5 112.9 m.), registering the highest level for the last 10 years. But at the end of the period under review the deficit registered abrupt increase, exceeding USD 2 billion (calculated on FOB export/CIF import basis) and reaching the previous year volume (USD 2.15 billion). Direct foreign investments for 2002 amounted to only USD 458 m., registering a decrease by USD 354.9 m. compared to 2001. The business environment in the energy sector improved, however big investments were not attracted. In 2002 structural changes in the transport sector developed at a slow pace and the long-awaited entry of private initiative in the use and maintenance of transport infrastructure did not become a fact. The past year brought a number of changes in the legislative framework of high technology and communications, yet at the same time the business registered unsatisfactory (according to many company managers) results. Throughout the year tourism was among the sectors registering the highest levels of development - the inflow of tourists to Bulgaria and the proceeds from tourism increased, notwithstanding the overall unfavorable trends in a global aspect. The general macroeconomic stabilization of the country in 2002 and the start of negotiations with EU on Chapter Agriculture created favorable preconditions for restructuring of a number of agrarian sub-sectors on the way towards successful completion of the transition to market

relations. Several positive trends were observed on the capital market throughout the year - a start was given to the exchange trade in compensatory instruments, the SOFIX index reached higher levels, market capitalization increased. The state of banks in Bulgaria remains stable, with excellent measures of capital adequacy and liquidity, and a well-functioning banking supervision. Yet at the same time the banking sector of Bulgaria remains relatively small in terms of the assets and the share of provided loans in GDP. The past year can be characterized as a period of transition in Bulgaria's social policy and of efforts to achieve better coordination of economic and social policy in the future. The number of registered unemployed indicator definitely registered a positive trend in 2002. Throughout the year discussions in the healthcare sector were focused on the amendments to the Health Insurance Act, on the Minister of Healthcare's refusal to sign the annex to the 2002 National Framework Agreement, on problems with the money for medications, which were exhausted as early as mid 2002, on the amendments to the Human Medications and Pharmacies Act. The healthcare reform is practically in a standstill. Several focus points of 2002 Bulgarian environmental policy were outlined throughout the year: the progress of negotiations on Chapter 22: Environment; the passing of a new framework law - the Environment Protection Act, of a new Biodiversity Act, of regulations on the application of the Chemicals Act and the Waters Act, as well as the progress in the implementation of basic environmental principles in agriculture. 2002 negotiations for Bulgaria's accession to EU resulted in 23 temporary closed chapters. The 2002 Regular Report of the Commission on the Progress of Bulgaria stated for the first time that the country is a functioning market economy. Throughout the year the Government undertook certain initiatives to improve the business environment, however implemented measures do not have an unambiguous effect and, overall, entrepreneurs do not see any material improvement of the conditions for doing business.

The Estat Index of Business Climate in Bulgaria (April 2002 – January 2003)

During the period under review the **Estat Index of Business Climate in Bulgaria** remained within the neutral portion of the scale (with a range of -100 up to +100): from -0.998 (April) to -2,55 (January), according to which the condition of business environment can be defined as neither favorable, nor unfavorable. Due to the great width of ranges, the negative sign is mainly of psychological significance.

April 2002

The expert evaluation of the value of each **Estat Index** component for the condition of business climate reveals that Component I "General Condition of the Company" has the greatest weight. However, the negative value of Component III "Business Environment" proved decisive for the general estimate and for the negative sign. Actually, the negative attitude towards the business environment is due in the first place to the fact that business environment problems are mainly identified with the role of the State.

Major problems encountered by entrepreneurs concern administration, legislation, tax system, corruption. Ninety three per cent of the businessmen state that work with the administration is quick and efficient only when you know somebody there. Ninety two per cent agree that it is difficult to start up new business in Bulgaria. Eighty five per cent are of the opinion that changes of legislation are too frequent, and 80 per cent believe that tax policy makes companies to evade taxes. More than 75 per cent of the respondents state that most entrepreneurs are ready to give extra money as a bribe to avoid administrative barriers.

The Government policy for promotion of business activity is given a negative assessment. Sixty four per cent of the interviewed think that the Government does not encourage business development.

The above data lead to the conclusion that entrepreneurs give somewhat abstract assessment of Bulgarian business environment. Expectations for the future are positive, there is overestimation against competitors of one's own capacity and level of development. At the same time assessments of the state of businesses are mainly neutral, or with a slight prevalence of negative estimates.

Nevertheless, a high tendency to invest is registered among managers. At the same time, detailed data reveal that many Bulgarian entrepreneurs give a priori answers to economically fundamental questions. Stereotypes, which often resemble the skeptic theses of the public rather than the pragmatic assessment of business circles, are reproduced. The survey revealed that the interviewed are influenced in their answers by

the desire to present their company in a more favorable light - with adequate resource support and competent management.

One might say that the high tendency to invest is rather of a declarative nature and is not a result of the actual capacity of companies, because 70 per cent of the respondents admit that they experience shortage of financial resource in their day-to-day operation.

July 2002

The assessment of the snapshot condition of companies was not very favorable - every fourth interviewed defined it as rather worse, and every second - as satisfactory. The assessment remains practically unchanged compared to the beginning of the second quarter.

The tendency to invest remains high, though 67 per cent of the businessmen state that they experience shortage of financial resources in their operation and give an average rating of 3.30 to their available cash resources (on a scale of 2 to 6).

The tendency to overestimate against competitors one's own capacity and level of development persists, though estimates of the current state of companies and available resources are not high.

More than 92 per cent of interviewed managers definitely think that it is difficult to start up new business in Bulgaria. Ninety six per cent of companies have put into practice continuous quality control of products and services and corporate strategy updating. The share of entrepreneurs who are willing to take a bank loan to invest has dropped down by more than 10 per cent, but nevertheless it remains high (almost 60 per cent).

Entrepreneurs encounter several major problems in their operation. Bureaucracy is stated first. Almost 89 per cent of the interviewed think that work with the administration is quick and efficient when you know someone there. Eighty eight per cent of the respondents rate as the second major obstacle the change of the legislative basis. Unfair competition impedes corporate development according to 85 per cent of the interviewed. Administrative barriers generate corruption. Seventy eight per cent of the respondents think that a great part of Bulgarian businessmen would pay extra money to avoid problems.

October 2002

Despite the registered static nature of business climate, certain **Estat Index** components preserve a downward trend in terms of values. Unlike the previous period under review (April - June) when the decrease was due to a seasonal drop in the optimistic expectations about the next quarter, the present index value decrease is a result of the clearly manifested tendency to reassess investment attitudes, i.e. of a change in the second

index component "Investment attitudes and Corporate Strategies".

The share of the interviewed managers who would take a bank loan to invest dropped down by 8 percentage points compared to the period January - April when a drop by almost 16 percentage points was registered. The decrease is rather due to lowered trust in the banking system or to negative assessment of the conditions offered by lending institutions rather than to unwillingness to develop the core business. Such an assumption is supported by the fact that the share of respondents who agree with the statements concerning investments only, such as "If I had available funds, I would invest them in some other activity, notwithstanding the risk", or "If I do not have funds to invest in the core business, I would do my best to secure them", does not register any drop. There is actually no difference between July and October values in terms of these statements.

The tendency to invest decreased, though change in the available ready money was not registered.

A clear downward trend is only observed with respect to the share of respondents who would take a bank loan to invest. The other statements comprising Component II "Investment attitudes" of the **Estat index** preserve the same or similar values.

A decrease of the tendency to overestimate against competitors one's own capacity and level of development is observed. The share of managers who think that their company does not have any competitive advantage registers a decrease, although the estimate of available resources remains unchanged.

The extremely critical attitude of the business towards Government policy, legislation, tax system, and administration is preserved in the third quarter as well. For three months the share of the interviewed who agree with the statement that the Government promotes business development has dropped down from 17 to 9 per cent. The lower share of respondents who think that the Government implements a policy for support of research and the use of high technologies is in harmony with the above statement.

January 2003

Component II ("Investment attitudes") of the **Estat Index** registers continuous decrease of the tendency of Bulgarian companies to invest, with the trend observed in previous surveys preserved. Given such a dynamics, in the months to come the value may well move from the positive (+20 to +60) to the neutral portion of the scale (+20 to -20).

Assessment of the general condition of economic actors reveals a downward trend, labor market potential decreases,

discontent with Government's policy with respect to the business increases.

The dissatisfaction with legislation, administration and existing corruption expressed in the previous months is preserved in the beginning of 2003.

The basic focus points in Estat Agency's surveys of the business climate in Bulgaria are illustrated in the following figures and tables.

Figure 1. Business climate dynamics

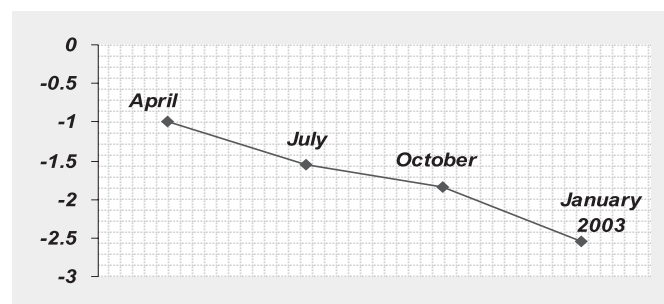


Figure 2. Investment attitudes dynamics

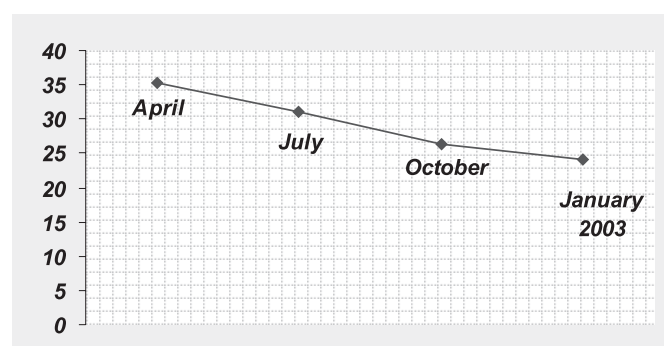


Figure 3. In your opinion, has the condition of your business changed throughout the months? (in %)

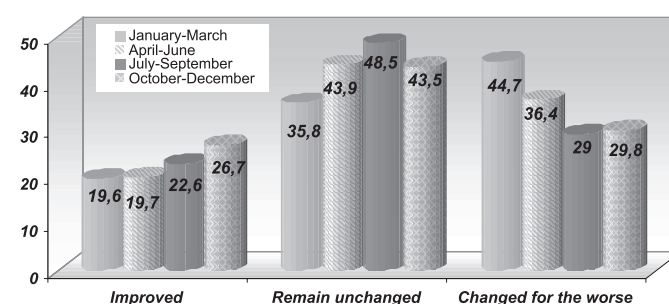


Figure 4. How do you assess the current state of your business? (in %)

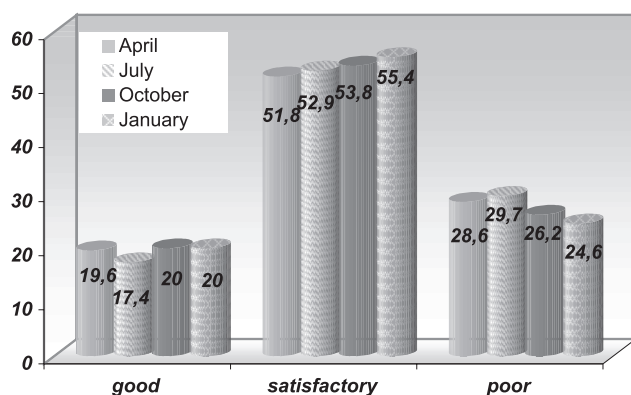


Figure 5. Will the state of your business change throughout the months? (in %)

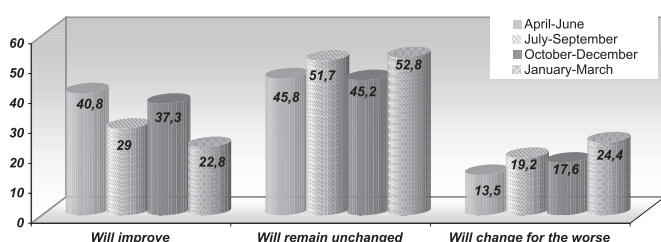


Table 1. Trends in some statements concerning investment attitudes (share of positive replies), %

STATEMENTS	2002			2003
	April	July	October	January
If I do not have funds to invest in the core business, I would do my best to secure them	89.6	84.6	84.1	83.0
I would take a bank loan to invest	67.8	59.9	52.0	55.8
I can easily find the workers and employees I need	56.4	60.4	51.3	48.3
I have partners on whom my business is dependable in a long-term perspective	56.5	53.8	50.6	46.3
I prefer to export (I would rather export) to the international market, because I cannot realize such proceeds in Bulgaria	38.2	35.8	35.0	33.0

Table 2. Trends in some statements concerning the business environment (share of the interviewed who agree with the statements), %

STATEMENTS	2002			2003
	April	July	October	January
It is difficult to start up new business in Bulgaria	91.9	92.4	91.2	88.6
Working with the central and local administration is easiest when you know someone there.	92.8	88.5	88.5	88.9
Most businessmen would pay more to avoid problems with the administration	78.3	77.9	79.3	80.7
The Government implements a policy in support of research and the use of high technologies	16.3	17.6	12.3	12.6
The Government promotes business development	12.4	16.6	9.1	9.4

Business Environment According to Estat Agency Surveys

Results of quarterly surveys of entrepreneurs carried out during the year do not reveal any significant changes in business environment assessments. Problems outlined as early as the beginning of the year persist. Start up of new business, work with the central administration, lack of consistency of legislative initiative, and unfair competition are given the most negative assessments. The interviewed remain critical about the efficiency and impartiality of the judicial system, public procurement procedures, the absence of well-directed policy for promotion of the technological and innovative development of businesses.

The overall conclusion is that business circles were most optimistic in the beginning of the year, however, some indicators register the highest positive assessments in early summer. The tax sphere seems to be the area registering positive change throughout the whole year. Entrepreneurs' assessments of this indicator reveal an upward trend - opinions were most negative in the beginning of the year, and more positive in the latest survey carried out in January 2003.

Administrative barriers and start up of new business

The conditions for the start up of new business in Bulgaria remain the indicator registering the lowest estimates in surveys throughout the whole year. Consensus here is high - around 90 per cent of the interviewed assess the conditions for the start up of new business as rather difficult, and the value remains at this level since the first surveys. At the same time there is certain drop in the number of respondents who definitely think that administrative barriers are the most serious problem for the business - from 92 per cent in the first quarter to 88 per cent in the fourth quarter.

A look at some objective facts - data¹ from the World Bank, for example, reveal that the value of the documents for start up of new business in Bulgaria amounts to USD 120, or 6 per cent of the GDP per capita. In other CE countries, Hungary for example, the USD 3120, or 66 per cent of the GDP per capita, are required. This means that the start up of new business in Bulgaria is not so expensive, i.e. objective facts are not so unfavorable. This discrepancy of estimates could be explained in part by certain force of habit in entrepreneurs' replies and tendency to dramatize.

Besides, surveys by the Center for Economic Development reveal that municipalities which have introduced the "one-stop shop" service have largely overcome administrative barriers and the local business do not point out this problem. Of course, the radical settlement of the problem of licensing barriers and the start up of new business still lies ahead.

Institutions and Government

The share of entrepreneurs who definitely believe that the Government implements a policy for business promotion remains small - only 9 per cent in the fourth quarter, with registered decrease compared to the first and the second quarters when the values were 12 and 16 per cent, accordingly. More optimistic results could be expected in the future, provided that the Government implements the package of measures to encourage economic growth, announced in October 2002. Some measures are targeted exactly at the promotion of entrepreneurship - further reform and simplification of regimes, accelerated bankruptcy procedures, set up of free industrial zones, tax reliefs therein, etc.

A slight increase of the share of respondents who think that the Government exercises consistent legislative initiative is observed - the share of the interviewed who agree with this statement varies within the range of 13 and 18 per cent, and in the fourth quarter it is 16 per cent - by a couple of percentage points higher compared to the previous quarter. The status quo in terms of whether the legislative basis creates equal opportunities for all economic subjects remains throughout the year at the level of around 17 per cent. A positive change is observed in terms of the practical application of regulations - in the first quarter 79 per cent of the interviewed believed that this was a difficult process, whereas in the fourth quarter the value dropped down to 72 per cent.

Relations with the central administration

The share of entrepreneurs who think that relations with the central administration are best settled "when you know someone there" registered a slight decrease from 93 to 88 per cent. In principle these relations generate corruption. The share of managers who are ready to pay extra money

to avoid problems with the administration remains generally the same - around 80 per cent. There is great difference in the assessments of corruption by various institutions and non-government organizations, but the corruption environment registers certain change for the better. This fact was also reflected in the latest Global Competitiveness Report of the World Economic Forum. It is this field that registered the most significant positive change - Bulgaria moved to the upper half of the countries with lower corruption level.

Competition on the domestic market

The share of respondents who believe that there is unfair competition in the country, which impedes the business, remains within the range of 79 to 85 per cent. The share of the interviewed who definitely consider it a serious problem registered its highest values in the last quarter. The effect of the amendments to the Competition Protection Act and the newly passed State Aid Act is to be felt yet.

The percentage of the interviewed who definitely believe that public procurement procedures are transparent and clear remained at lower levels throughout the year - around 10 per cent, with a drop down to 8 per cent in the latest survey. A conclusion can be made that the amendments to the Public Procurement Act do not have any material effect on the transparency and impartiality of procedures. The new 2003 amendments may contribute to acceleration of these procedures.

Tax environment

As mentioned above, it is tax environment that has registered the most positive changes in entrepreneurs' assessments. There are several questions in the surveys, which concern these problems and the answers to these questions justify such conclusions. In April 10 per cent of the interviewed definitely agreed with the statement that the tax system created equal conditions for the business, whereas in the last quarter the share of the interviewed who thought this way increased to 15 per cent. Other positive conclusions are also confirmed - for example, the share of the interviewed who assess the patent tax as unbearable registers a decrease from 57 per cent in the first quarter to 50 per cent in the latest survey. The share of respondents who definitely think that tax rates are high and generate tax evasion decreased (from 80 per cent in April 2002 to 71 per cent in January 2003). Opinions about social security and health insurance contributions register a similar trend - the share of entrepreneurs who think that these contributions are a serious burden for the business has decreased from 64 to 61 per cent. Assessments of the profit tax rate also register a positive change - in January 32 per cent of companies think that the tax is bearable, whereas in the previous quarter only 23 per cent agreed with this statement.

¹ Cited in the 2002-2003 Global Competitiveness Report of the World Economic Forum.

It is notable, however, for all questions concerning the tax environment, that entrepreneurs' opinion was most positive in the second quarter. The general positive trend could be a result of higher level of predictability and making companies able to plan the taxes due.

Policy to encourage technological and innovative development

Unfortunately, assessments of the policy to encourage technological and innovative development have remained quite negative since the first surveys. What is more, the share of entrepreneurs who do not see such a priority outlined increases reaching a level of 83 to 88 per cent.

A Research Promotion Act has been developed. Its promulgation would probably lead to introduction of rules of greater clarity, targeted at project financing promotion and closer link between research and business.

European integration

The share of entrepreneurs who think that harmonization of Bulgarian with European legislation will improve the conditions for doing business in Bulgaria has decreased throughout the year, which is a disturbing fact. Overall, the percentage of positive assessments remains at rather low levels - between 47 and 55 per cent. But it should be also noted that the latest survey conducted in January 2003 registered an abrupt increase of the number of interviewed who agree with the statement about the positive role of harmonization from 47 per cent in the third quarter to 54 per cent. A possible explanation could be the assessment for Bulgaria as functioning market economy and the adopted road map for Bulgaria's accession to the EU, as well as the fact that more information on this processes was provided in the last few months.

Nevertheless, the percentage of the interviewed who tend to give positive assessment of the role of European integration remains at low levels and this fact confirms again the need to provide more information about the progress of harmonization and the opportunities it generates.

Several **summarizing conclusions** have been made on the basis of the four surveys conducted in the previous year:

Unfavorable trends:

- Negative assessments of the conditions for start up of new business are preserved;
- Entrepreneurs' opinion about the transparency and impartiality of public procurement procedures remains negative;
- Market competition is not sufficiently intensive and fair;
- High level of distrust in the impartiality of the judicial system is observed;
- The policy for technological and innovative development is not a priority;

- Business circles' skepticism about the benefits and opportunities provided by the European integration process generates serious concern.

Some positive trends:

- Tax environment is given a more positive assessment;
- Positive change of corruption environment is observed;
- Certain improvement of the attitude towards the practical application of regulations is observed;
- The banking system is assessed as stable and reliable; certain revival of the lending activity is observed.

NSI's Business Surveys

General business climate indicator²

The economic situation in 2002 is somewhat better compared to the previous year. The progressive increase of general business climate indicator values from January to May 2001 is indicative of quick and material improvement compared to 1999 and 2000. But at the end of 2002 the integrated opinion of industry, construction and retail trade business circles about the economic situation, measured by the general business climate indicator does not seem to differ much from that in mid 2001 when a trend of stagnation in economic situation dynamics was outlined. Stagnation could be interpreted on one part as a symptom of "difficulty to maintain" achieved improvement in a situation of readjustment as a result of the cheaper dollar, and on the other part as "gaining momentum" for the next progressive improvement, which could be induced by a possible considerable improvement of the manageable internal environment and provided that an abrupt change for the worse of external factors does not occur.

Figure 6. Business Climate (NSI)



Source: NSI

² NSI conducts business surveys in accordance with the harmonized EU program. Answers to the questions in the surveys are presented on a three-range category scale of the type: "increase", "no change", "decrease", or "above the normal", "normal", "below the normal". Balances of estimates are calculated as a difference between the relative shares of the extremal variants of an answer. The business climate indicator is a geometrical mean of the balances of estimates for the current business situation and the expected business situation of enterprises in the next 6 months. The general business climate indicator, commented in this paper with a view to make a comparison with the corresponding quarter of the previous year, is a weighted arithmetical average of three branch business climate indicators: those of industry, construction, and retail trade. As of January 2003 NSI started to present the general business climate indicator including the business climate indicator values in the service sector.

Industry

The industrial business climate indicator manifested a downward trend from the beginning of the year till June mainly as a result of the lower estimates of current business situation. Nevertheless, since January an upward trend of expectations for exports in the next months has been observed, which could be interpreted as higher determination of industrial circles for market breakthrough. The abrupt improvement of business climate in industry in July is related in the first place to the higher export expectations of enterprises. Overall, the level of orders decreased compared to a year ago. Nevertheless, the rather smoother and upward since the middle of the year fluctuation of monthly estimates of order levels (both in the country and from abroad) contribute to certain stabilization of the business climate in industry.

Figure 7. Business Climate in Industry (NSI)



Construction

NSI's business surveys reveal that the year 2002 was somewhat better for the construction sector compared to 2001, with both years registering considerably higher levels and quite similar curves of business climate and current construction activity indicators compared to previous ones, which could be interpreted as higher stability of the economic situation in the sector.

Figure 8. Business Climate in Construction (NSI)



Retail trade

Unlike industry and construction, in 2002 the business climate in trade remained at nearly the same levels as in 2001 and rather below the 1998-2000 levels.

Figure 9. Business Climate in Retail Trade (NSI)



Gross Domestic Product

Annual economic growth may well be higher than the latest official growth estimates of 4.2 per cent³, given the real growth of 4.4 per cent for the first nine months of the year and an estimated growth of not less than 4.2 per cent for the fourth quarter.

Expectations are supported by the favorable data from NSI's monthly surveys for the period since the beginning of the year. On one part, in the period January-December the level of industry sales is lower than that for the corresponding period of 2001, the growth of industry output is 2.6 per cent on an annual basis (with a growth of 0.7 per cent for the period January-November 2001).

Table 3 . Volume Index, Corresponding Period of the Previous Year =100, %

	I-XII'2001	I-XII'2002
Industrial production	100.7	102.6
Industrial sales	99.4	99.8
Domestic trade, total, net sales	100.1	104.3
- Trade of motor vehicles and motorcycles, repair of motor, retail trade of automotive fuel, net sales	103.3	101.7
- Wholesale trade, net sales	98.5	104.9
- Retail trade, repair of personal belongings and household goods, net sales	104.9	103.2

Trade sales growth is much higher (4.3 per cent for the period January-December on an annual basis, with 0.1 per cent for the period January-December 2001). The permanent high business climate levels in the services sector, which has the highest structural effect on GDP growth and manifests the most stable growth rates in 2002, give grounds to expect a high level of growth in the sector in the fourth quarter of 2002 and for the year as a whole.

In terms of GDP consumption, further growth of individual consumption is expected, which is promoted in particular by the decrease of the number of registered unemployed by more than 40 thousand people in the period October-December 2002.

Further growth of investments is also expected, though at a lower rate. On one part, there is sustainable growth of loans to private enterprises. Furthermore, according to NSI's investment business survey conducted in industrial enterprises⁴ in the second half of October, the nominal increase of investments in industry in 2002 compared to the previous year is estimated at 7.2 per cent.

A further argument in support of the positive expectations about Bulgarian economic growth in the fourth quarter and for the

year as a whole is the fact that a further acceleration of growth in world economic centers is observed (according to data for the third quarter of 2002). The positive effect for the Bulgarian economy is observed in the higher growth of the export of goods and services compared to the import (in the second and third quarter of 2002).

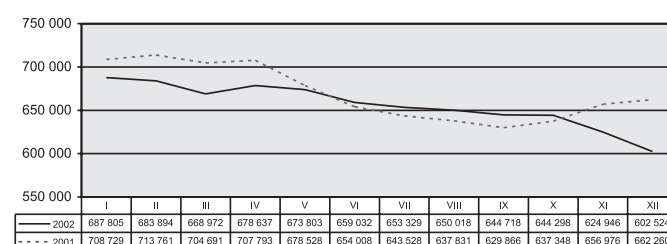
Inflation

Notwithstanding the more significant monthly rise of prices in the beginning of the year, the 2002 price increase manifests lower rates compared to the two previous years. The 2002 average inflation rate on an annual basis is 5.8 per cents (manifesting a decrease since 2000), the accumulated annual inflation - December 2002 compared to December 2001 - is 3.8 per cent, which is the lowest level since 1999. Average food prices on an annual basis are by 4.2 lower compared to 2001, but a significant average increase on an annual basis of non-food (+10.4 per cent) and service (+11.4 per cent) prices is observed.

Labor Market

For most of the months in 2002 the number of the unemployed is lower compared to the corresponding months of the previous year, but the average number of unemployed decreased by only 14 thousand people (or by 2 per cent) on an annual basis.

Figure 10. Number of Registered Unemployed



Source: EA

According to data from the labor force monitoring, the average number, taken on an annual basis, of the people who define themselves as unemployed manifests considerable decrease by almost 11 per cent, but the average number, taken on an annual basis, of the manpower reserves⁵ decreased by 5.4 per

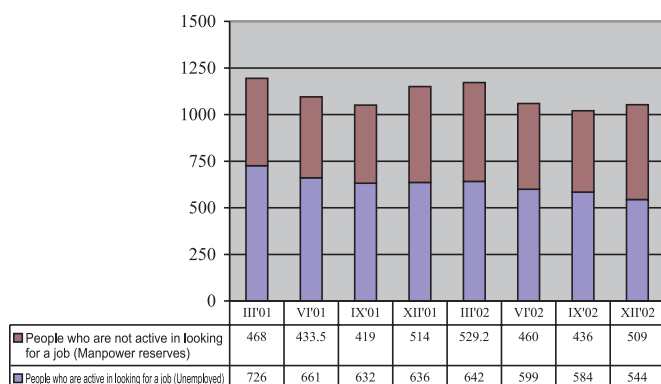
³ Source: MoF, 22 January 2003, Preliminary Report on the Performance of the 2002 Consolidated Fiscal Program <http://domino.minfin.government.bg/news/Archive-BGn.nsf/1e21197594cc865c4225686000394a45/080adf96ba152a7842256cb600484962?OpenDocument>

⁴ In October 2002 NSI conducted its first investment activity monitoring in industry, which was completely harmonized in accordance with the European Business and Consumers Monitoring Program, and with EC's investment survey in particular. The basic objective of this monitoring is to collect information about the expected growth of investments in industry in the current year compared to the previous year, and about the expected growth of investments in the next year compared to the current year. In its recent practice NSI calculated expected rates entirely on the basis of forecasts from enterprises, and consequently the data about the previous year were underestimated, which resulted in overestimated rates. In the October 2002 survey NSI makes use of information about investments in the previous year based on final data by the enterprises.

⁵ People at the age of 15 to 64 years, who are willing and ready to work, but do not actively look for a job.

cent, and consequently the average number of economically active people who do not have jobs but are willing and ready to work decreased by 4.1. per cent.

Figure 11. Unemployed People Who Are Willing and Ready to Work, Thousands

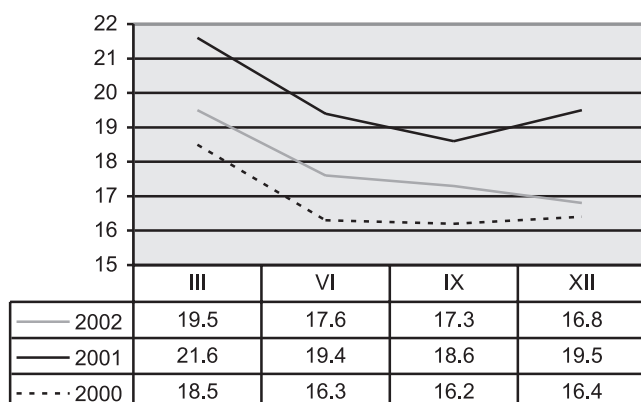


Source: NSI

The labor market supply and demand ratio⁶ improved in 2002. In December 2002 the active labor supply (employed + unemployed) exceeded demand (employed + free jobs) by 18.7 per cent, compared to 23.6 per cent for December 2001; reciprocally, demand covers 84.3 per cent of supply, compared to 80.9 per cent for December 2001. On the other hand, at the end of 2002 labor demand covered 72.8 per cent of possible labor supply (employed + unemployed + manpower reserves), compared to 69.97 per cent for December 2001.

According to data from the labor force monitoring, 2002 unemployment levels are lower compared to the previous year, but higher compared to 2000. Nevertheless, unemployment preserves a downward trend throughout the year.

Figure 12. Unemployment according to Labor Force Survey, %



⁶ Ratios are indicative. Combined data from NSI's LFS of employed, unemployed and manpower reserves and EA's data about free jobs as of end of December.

The main objectives of the fiscal policy in 2002 were the maintaining of a balanced budget, low budget deficit and fiscal stability. These objectives were met through reasonable spending observing the main principles of fiscal sustainability.

According to the first data about the implementation of the 2002 fiscal program the basic budget parameters have been fulfilled. The government reports stable management of public expenditures in observance of strict fiscal discipline and raising the efficiency in the implementation of the revenue side of the budget.

According to preliminary data the actual deficit was BGN 218.3 million which is 0.7 per cent of the GDP, while the planned deficit was BGN 257.3 million, that is 0.8 per cent of the GDP. This is a better level of the balance and it is by 0.1 point lower than the one planned in the program. The achievement of such a low deficit is the basis for attaining economic stability, and the economy growth is expected to be over 4.2 per cent.

The improved balance is due to over-fulfillment of the revenue side of the budget as compared to the program for 2002. The over-fulfillment is due most of all to the revenues from custom duties, profit tax and non-tax revenues.

The past year is characterized also by the first steps made towards fiscal decentralization in Bulgaria. Fiscal decentralization is a lengthy process covering the whole system of financial relations at all public governance levels. Its main objective is to deliver public services of quality, quantity and prices adequate to the needs and payment potential of the citizens, on the basis of sustainable and long-term balance of the spending responsibilities of municipalities with steady revenue sources and efficient citizen control.

Fiscal decentralization should be based on the following principles:

- Setting up a system of incentives aimed at increasing the local revenues, strengthening the potential in the field of financial management and maximum extent of local autonomy in determining the essence and contents of municipal services;
- Simplified structure of financial relations;
- Strict financial discipline in the central and local governments;
- Possibility for the central government to monitor and evaluate the decentralization process;
- Taking into account the differences among municipalities in terms of their financial resources, management competencies and opportunity for municipalities with different potential to develop according to their own specifics;
- Conditions for efficient citizen control.

In line with the above are also the amendments made at the end of 2002 in a number of laws referring to municipal finance. Starting from 1 January 2003 the full amount of the income tax will remain in the budgets of 228 municipalities, and the other 35 municipalities specified on a list will receive a percentage of it.

The amendments to the Local Taxes and Fees Act are aimed at improvement of the administrative procedures with a view to minimization of the costs for tax administration and taxpayers. The amendments concerning local fees have taken into consideration the fiscal decentralization concept and will give a chance to the city councils to determine independently the base and amount of local fees taking into account the specifics of the costs of delivered services on the territory of the particular municipality.

In 2002 **the total amount of the government and government guaranteed debt** decreased by BGN 2,600 million, reaching BGN 18,180 million at the end of the year (recalculated on the basis of the BNB central exchange rates as of 31 December 2002) according to data from the Ministry of Finance. The increase in the total amount of the debt in the first quarter of 2002 was due mostly to the increase of the domestic debt and to a smaller extent to the US dollar value increase to the Bulgarian Lev. In the second quarter of 2002 there was a further decrease of the total amount of the debt. In the third quarter of the year there was an increase of the total debt amount by BGN 74 million, resulting mainly from the increased US dollar value compared to the Euro over the period. At the end of December 2002 the total amount of the government and government guaranteed debt was 56 per cent of the Gross Domestic Product (according to the updated estimate of the latter, as per data from the Ministry of Finance).

Compared only to the end of the third quarter there is a decrease in the total amount of the debt by BGN 748 million owing to an inconsiderable decrease of the portion of the debt denominated in dollars, accompanied, however, by substantial devaluation of the dollar to the Euro measured at the end of the two periods. The large drop of the ratio of the total debt amount as compared to the (estimate for) the GDP is among the best news relating to the government debt management. On the other hand it should be noted also that especially against the old data of the Ministry of Finance for the preceding months, the drop is partially explained by the positive adjustment of the 2002 GDP estimate, which was made at the end of the year. That is why it would be more adequate to report comparable data or directly the actual (instead of the estimated) GDP for the respective years.

In mid-2001 a categorical message was conveyed for change in the **foreign debt** management policy. Beyond the repeatedly announced objective for improvement of the ratio foreign debt : GDP (due to the structure of the Bulgarian government debt

this ratio is of crucial importance to the implementation of Maastricht Criteria), at present there are still no indications that this objective has been included in any long-term strategy for debt management. It was as early as in 2001 that the first evidence of the active current policy on foreign debt management occurred. First, this was the buy-back of Brady bonds under the foreign debt in the autumn of 2001, and second, in November 2001 Eurobonds were marketed of Euro 250 million face value and with maturity 1 March 2007. At the end of 2001, according to data from the Ministry of Finance, the foreign debt structure contained a debt in Eurobonds amounting to USD 220.3 million.

The active policy regarding the foreign debt continued in the first quarter of 2002 as well. In March a large-scale transaction was conducted for replacement of foreign debt Brady bonds with new global Eurobonds. The transaction included simultaneously buy-back of Brady bonds, their direct replacement by bonds in dollars or bonds denominated in Euro, as well as a net issue of such Eurobonds. The summary results from the Ministry of Finance stated a net decrease of Bulgaria's nominal debt by USD 80 million, release of collateral of USD 197 million, and savings on the basis of net present value amounting to USD 94 million. Brady bonds of total face value of approximately USD 1 327 million were substituted. The newly issued dollar Eurobonds had a face value of over USD 513 million, maturity in 2015, interest coupon 8.25 per cent on an annual basis with two annual interest payments and yield of 9.1 per cent until maturity on an annual basis. The newly issued Eurobonds denominated in Euro had a face value of Euro 835 million, maturity in 2013, interest coupon of 7.5 per cent on an annual basis with one annual payment and yield of 7.987 per cent until maturity on an annual basis.

In the second quarter of 2002 the concrete results from the transaction had already been reflected in the indicators of the foreign debt dynamics. As of the end of June, again according to data from the Ministry of Finance, country's debt in Eurobonds (denominated in Euro and in Dollars) was a total of USD 1,594.3 million, which meant an increase by USD 1,376.2 million compared to the end of the first quarter. On the other hand, only for the first two months of the second quarter of 2002 the foreign debt in Brady bonds decreased by USD 1,326.3 million.

The third quarter of 2002 brought about the latest for the time being indications of the new active policy in the current management of the foreign debt. In September another restructuring of the foreign debt was carried out, where Brady bonds were replaced by Eurobonds in US dollars (through opening of the existing March issue of bonds with maturity in 2015). The summary results of the Ministry of Finance as of the end of the third quarter showed that Brady bonds amounting to a total of USD 866 million were exchanged against issued dollar bonds amounting to USD 759 million. The official data showed

a gross decrease of our foreign debt by USD 107 million, and release of the collateral to the value of approximately USD 135 million. Thus only from the operations in September the net decrease in the foreign debt according to the Ministry of Finance amounted to approximately USD 242 million.

The afore-described operation was reflected in the debt dynamics in the fourth quarter of 2002. For the period from the end of September to the end of December our foreign debt in Brady bonds (principal and accrued interest) decreased by the amount equal to the value of the bonds substituted in September. Due to the newly issued dollar Eurobonds and the increased value of the Euro, our foreign debt in Eurobonds increased by USD 815 million in the period under review.

The foreign debt dynamics statistics in 2002 does not confirm firmly the positive effects of the operations undertaken for restructuring the debt. Nevertheless, however, such restructuring and active management of the foreign debt received a completely positive assessment by investors. This was also one of the reasons for the further increase of Bulgaria's credit rating in the fourth quarter of 2002. In the beginning of October the biggest Japanese credit agency Japan Credit Rating Agency (JCRA) assigned to Bulgaria a "BB+" rating with a positive prospect of the long-term debt in foreign currency (this was the first ever credit rating assigned to Bulgaria by JCRA). Again in the beginning of October the international Rating Agency Standard and Poor's increased its rating for Bulgaria (the rating of the long-term government-guaranteed debt in foreign currency) from "BB-" with stable prospects to "BB" with positive prospect. Again at the end of October the international agency Moody's improved the prospect of that same Moody's rating of Bulgaria's (bonds and long-term securities) – from stable to positive, with the unchanged rating "B1".

The **domestic debt** dynamics also started showing indications that an active policy for its management was in place in 2002, similarly to the above-discussed new policy for the foreign debt. In this case again, it is not quite clear to what extent this policy is a part of a long-term strategy for the debt management, however last year the much more active behavior of the Ministry of Finance resulted at the beginning in some surprises and the need of a new behavior on behalf of many of the participants in the money market in Bulgaria.

The beginning of 2003 is already dominated by the expectation that the government securities market and the money market will be a major priority for the Ministry of Finance in 2003, where portion of the domestic debt in the structure of the government and government guaranteed debt in general will be increasing. The two most important limiting factors for the development and management of the foreign and domestic debt will be the observance of the Maastricht criteria and the application of the Government debt Act adopted in September 2002 (discussed

here below).

Besides in terms of the sheer market effect, the actions of the Ministry of Finance and the lack of a strategy for debt management in 2002 have already been discussed also in the more general context of state governance efficiency. This is an interpretation of the recommendations in the Audit Office Report, distributed at the end of June 2002, about the audit conducted by the Ministry of the occurrence and management of the domestic government debt and the utilization of the debt instruments in 2001.

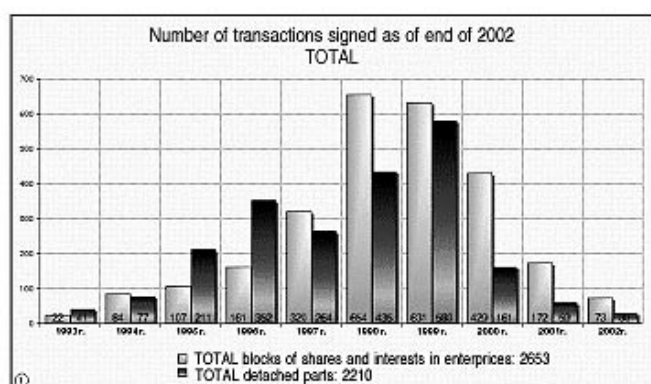
The recommendations of the Audit Office concerned three main areas. First, a new unit had to be set up with the Ministry of Finance to deal particularly with the domestic debt management. Second, the Audit Office report stated that the Ministry of Finance administration should specify more precisely the maturity of the newly issued securities, so as to achieve a smoother allocation of the burden of the domestic debt servicing in the following years. In its last recommendation in the report the Audit Chamber insisted on the adoption of a Government debt Act.

The Government debt Act was submitted to the Parliament as early as in January, but it was finally adopted in September 2002. This Act may be assessed positively, though just as a first step towards a possible long-term strategy regarding debt. This Act not only placed a systematic framework for all varied statutory instruments on debt, but it also introduced some legal norms which have been missing in Bulgaria for a long time, such as a definition of government debt, setting every next year the limits to the debt increase, establishing an official register of the government debt, advance notification to the Ministry of Finance in case of debt issue by municipalities, additional regulation of fiscal agent activities of the BNB, and many others. As it was stated by the proponents of the draft law in their justification, one of the more general objectives of such an Act is to cause a decrease in the costs for financing the budget.

Restructuring and privatization of the public sector continued in 2002. As of 31 December 2002, 53.25 per cent of the assets of state-owned enterprises, accounting for 80.64 of the assets subject to privatization⁷, were sold. Enterprises, which until recently were monopolists in the infrastructure sectors - energy, telecommunications, and railway transport, prevail in the group of state-owned companies.

The 2002 Annual Working Plan of the Privatization Agency sets out as privatization objectives 664 transactions, including sale of 238 companies where the State holds a majority interest⁸. As of 31 December 2002, the number of privatization transactions concluded was only 275, according to data by PA⁹. The annual plan is fulfilled at 41.4 per cent. The number of enterprises with majority interest sold is 73. The annual plan for these companies is fulfilled at 31 per cent.

Figure 13. Number of transactions signed as of end of 2002



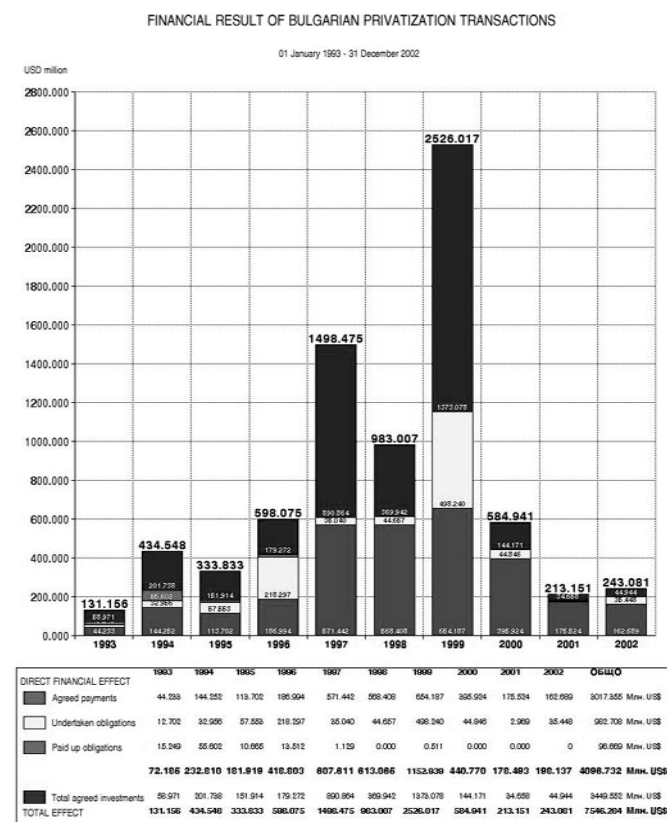
Source: PA, www.priv.government.bg

The conclusion is that 2002 was the worst year for Bulgarian privatization since 1995. If the current pace of privatization is preserved, the sale of the remaining around 400 companies where the State holds the majority interest will require another 5-6 years. None of the countries in transition witnessed a process of such a slow pace.

According to the Annual Plan, expected proceeds (agreed payments) from the transactions signed in 2002 are estimated at BGN 748 493 (in all legal payment instruments), including cash inpayments in the central national budget to the amount of BGN 618 523 thousand¹⁰. As of 31 December, PA reports a total financial effect of concluded transactions to the amount of USD 243 million. Agreed payments alone amount to USD 162.7¹¹.

Therefore a heavy under-execution of the revenue part of the Plan is also registered.

Figure 14. Financial result of transactions up to 2002



Source: PA, www.priv.government.bg

The failure of the Annual Privatization Plan can be attributed to several groups of reasons. The ruling majority developed and adopted with tremendous delay the new Privatization and Post-privatization Control Act. The President of the Republic of Bulgaria exercised his right to a veto and referred the act back to the National Assembly. It was put to the vote again and passed. Its final version was promulgated on 19 March 2002.

Major changes in the law include:

- Centralizing the privatization process in PA;
- Eliminating preferences; equality of buyers;
- Setting up of a special body - the Agency for Post-privatization Control;
- Creating a public register of transactions;
- Limiting to the minimum payments by alternative payment devices (compensatory instruments);
- Using open auctions and stock exchange offerings as basic privatization methods;
- Eliminating the possibility to re-negotiate clauses of privatization contracts already signed.

⁷ 2002 Operation Plan of the Privatization Agency, www.priv.government.bg

⁸ 2002 Operation Plan of the Privatization Agency, www.priv.government.bg

⁹ Report by Apostol Apostolov - Executive Director of PA, www.priv.government.bg

¹⁰ 2002 Working Plan of the Privatization Agency, www.priv.government.bg

¹¹ Report by Apostol Apostolov - Executive Director of PA, www.priv.government.bg

With the enforcement of PPCA, the share of the state in the capital of all commercial companies, with the exception of those listed in an annex to the act, is considered declared for privatization. According to PA data¹² the state interest in 2002 companies is declared for privatization. The companies where the state is a majority shareholder are 450, 20 are mixed, minority blocks of shares in companies privatized (over 50 per cent of the shares) in the first wave of mass privatization are 180; blocks of shares/stocks in companies for which privatization transactions were already signed amount to 1350.

The weak points in PPCA, which delay the privatization process, include:

- Declaration of all companies for privatization is actually non-declaration, because investors' interest is not attracted to specific companies, which are ready for privatization;
- The concentration of the thousands of minority interests in PA actually hides them from potential investors, because nobody makes a list of these interests, nor offers them for sale;
- The concentration of all transactions in PA makes line ministers and ministerial teams disinterested in privatization and they do not provide adequate assistance to PA in the preparation of companies for privatization.

The need to transfer documents from ministries to PA, the unexplainable claims of ministries and individual MPs to place new companies on the so-called "prohibition list" impeded the privatization process and limited PA's powers for prompt sale of companies.

The declared desire of PA's executive management to sell blocks of shares in privatized companies and companies under privatization through the stock exchange met the unwillingness of the Executive branch and the Legislature. That resulted in an undetermined policy for the use of alternative payment instruments - continuous drawing up of lists and putting off the privatization of blocks of shares in different companies via the stock exchange.

The enhanced attention of the prosecutor's office and the special parliamentary commission to old transactions and procedures generates excessive caution in PA employees and delays the pace of preparation of transactions. At the same time, continuous requests by the economic police, the investigation office and the prosecutor's office for information and explanations on old transactions take bulk of PA employees' time.

A disturbing trend, which was observed in the third quarter of 2002, is worth noting. Different proposals for amendments to the newly passed PPCA are introduced in the National Assembly. A major criticism towards the repealed privatization

act concerned the numerous (over 30) amendments in the ten years of its effectiveness, which considerably altered its basic idea and impeded its application in practice.

Government's expectations to finalize the two biggest privatization transactions - of BTC EAD and Bulgartabac - Holding AD, did not come true. The preparation of these transactions was delayed because the new PPCA was passed behind schedule and the Parliament approved with delay the privatization strategies for these companies. The procedure for Bulgartabac - Holding was opened on 25 March, and that for BTC EAD - on 2 April, 2002. The two procedures were accompanied by repeated extension of time limits, which generated a negative social effect and suspicions about legal violations. Later PA's decisions were attacked in court, which further complicated and prolonged the procedure. Thus at the end of 2002 the privatization of BTC and Bulgartabac was not completed yet. That influenced the overall execution of the revenue part of the Annual privatization plan.

The disinterest of foreign investors to participate in the privatization of Bulgarian companies can be explained by the low levels of international investment activity, but the number of transactions with the participation of foreign investors does not correspond to the priorities set forth in the Government program. Overall, the work of the Foreign Investments Agency in 2002 can be given a negative assessment. The opportunities provided by the Foreign Investments Act are not made use of, which has direct effect on the absence of foreign investors.

The lack of correspondence and clarity in PA's actions in the sale of big companies, as well as the inconsistent signals coming from the parliamentary group of National Movement Simeon II have extremely negative effect on the investment climate. There is an obvious a need of both political will and continuous efforts to present the companies ready for privatization to interested foreign investors.

¹² 2002 Working Plan of the Privatization Agency, www.priv.government.bg

The year 2002 was not marked by any significant improvement of the conditions for doing business in Bulgaria. Nevertheless, Government support to small and medium-sized enterprises was manifested in the National Strategy for Encouragement of SME Development in Bulgaria 2002-2006 accompanied with an Working Program, which was approved by the Council of Ministers on March 28, 2002; in Bulgaria's accession by Decision No. 185/1 April 2002 of CoM to the Multiannual Program of Enterprises and Entrepreneurship, Particularly Small and Medium-sized Enterprises (2001-2005); in the Interministerial Group at ASME on Optimization of Regulatory Regimes with a View to Improve the Administrative and Regulatory Environment for the Business, set up by CoM in February 2002; and in Bulgaria's accession to the European Charter for Small and Medium-sized Enterprises (SME) on 23 April 2002.

The major objective of the National Strategy for Encouragement of SME Development is to create a favorable environment and conditions for development of a competitive SME sector, which will enhance the economic growth of the country while preserving the macroeconomic stability. The Strategy contains **seven basic priorities**, which focus on developing stable and transparent regulations for SMEs; implementing a policy to improve the financial environment; promoting the introduction of modern technologies and contemporary business models in the sector; improving the access of SMEs to foreign markets; efficient information and consulting services; and implementing a policy to improve the conditions for development of the business in a regional aspect. The priorities, which reflect the problems in the SME sector, are formulated in the Strategy in the following way:

- Simplified administrative and regulatory environment for SMEs;
- Improved financial environment;
- Support to innovations and technological development;
- Europeization and internationalization of SMEs;
- Improved access to information and services;
- Creating conditions for the development of SMEs in regional aspect;
- Promoting entrepreneurial spirit and skills

The Working Program is an integral part of the Strategy. It gives the short-term (till the end of 2002), mid-term (2003 - 2004) and long-term (2005 – 2006) initiatives in accordance with above priorities. The strategy highlights the role of institutions and **it is noted that the government, non-government organizations, and the society as a whole are responsible for the creation of a favorable environment for SMEs.**

By Decision No. 185/1 April 2002 of CoM **Bulgaria joined EU's Multiannual Program of Enterprises and Entrepreneurship, Particularly Small and Medium-sized Enterprises (2001-2005).** ASME was appointed national program coordinator. The basic objective of the program is to encourage small and

medium-sized enterprises.

The multiannual program has five priority objectives:

- To promote business growth and competitiveness in the globalized knowledge-based economy;
- To encourage entrepreneurship;
- To simplify and improve the administrative and regulatory framework for the business, particularly for research, innovations, and the start up of new business;
- To improve the financial conditions for the business, particularly for small and medium-sized enterprises, and
- To provide the business with better access to EU services, programs, and networks; to improve their coordination.

The efforts of the Interministerial Working Group on Optimization of Regulatory Regimes set up by CoM in February resulted in **review of 361 regimes and a decision to amend nearly 200 of them - to repeal 73 and ease the other 120.** A start to the building of a Public Register of Regulatory Regimes was given in the middle of the year.

On 23 April 2002, at a special conference organized in Slovenia, **Bulgaria joined the European Charter for Small and Medium-sized Enterprises.** The Agency for Small and Medium-sized Enterprises is expected to get involved in the Charter's implementation in Bulgaria by way of coordinating the development of information materials.

With a view to facilitate the access of small and medium-sized enterprises to loans and on the basis of Decree No. 213/28 September 2001 of CoM on providing targeted financial support to entrepreneurs by way of micro-credit guarantee schemes, the Ministry of Labor and Social Policy developed the **Micro-credit Guarantee Fund Project.** The Pilot Project was launched on 26 December 2001 in 18 municipalities on the territory of 9 regions, and became operative countrywide as of August 2002.

The basic project objective is to create new jobs by facilitating the access of small and start-up companies and of physical persons to free financial resources necessary for development and expansion of their business. The project performs very important social functions such as alleviating the social tension in regions of high unemployment rates, creating prerequisites to financially strengthen and expand operating and start up small businesses, and creating favorable conditions for disabled people and other disadvantaged groups to start up their own business.

The tendency to avoid the implementation of tax policy targeted at the support of small and medium-sized enterprises, which are the basic source of employment in the country, was preserved in 2002, hence the need of further Government efforts in this field. The actions taken to reduce administrative barriers and facilitate the access to loans are definitely important for the SME sector. The wider application of the "information desk"

approach by municipal authorities is a positive development towards improving the administrative environment for business development. There is a need to improve the coordination of the government institutions, which are directly concerned with the implemented policy for support of the SME sector, whereby the efficiency of their actions would be improved. A national conference on SMEs would contribute to better systematize the problems in this field, to discuss corresponding measures, and to improve the efficiency of cooperation between the administration and representatives of the business and non-government organizations.

Foreign Economic Relations

It was inevitable that global economy slow down that started at the end of 2001 had a negative impact on Bulgaria's foreign trade – in the first six months of 2002 exports decreased by 6.6 per cent compared to the same period of 2001. Despite the strong dependence of Bulgarian economy on the condition of world economy, it managed to recover quickly and to make use of its competitive advantages in order to strengthen its positions in certain niches of international markets. Thus, from the beginning of the second quarter Bulgarian exports started promptly to grow and throughout the remaining months of the year their total value exceeded the levels registered for the same months of the previous year.

The annual volume of exports in 2002 (USD 5 578.1 m according to preliminary data and USD 5 750 m according to our estimates) exceeds by around 12.5 per cent the one in 2001 (USD 5 112.9 m). This is the highest value of exports for the last 10 years exceeding even the 1995 record (USD 5 354.7 m). If at that time the cause of increase was the entering into effect of the Provisional Agreement on Liberalization of Trade with EU, now, in addition to better access to markets, we can also mention the re-orientation of the economy towards production and export of consumer goods (clothing, shoes, furniture, medications).

Most strongly affected by the unfavorable conditions of foreign markets in 2002 was the export of energy resources (oil products, in particular) and it was the only export to mark significant shrinkage in terms of value (by 24 per cent) compared to 2001. Exports of raw materials and inputs was growing at a slower pace compared to these of consumer and investment goods, and the growth was mainly due to increased supplies of textile raw materials, timber and raw materials for food production, while metals and chemicals preserved their levels of 2001. Fastest growth in 2002 was marked by the exports of machinery and equipment (19 per cent) and consumer goods (15.6 per cent). All of this leads to **a change in the commodity structure of exports** – the share of energy resources dropped from 13.5 per cent in 2001 to 9.4 per cent at the expense of the increased share of consumer goods (from 33.5 per cent to 35.6 per cent), raw materials and inputs (from 40.8 per cent to 42 per cent) and investment goods (from 12.2 per cent to 13.3 per cent).

In terms of the **geographical structure of exports** the most clearly manifested feature in 2002 was the increase of the share of countries and regions with which Bulgaria has signed free trade agreements. Thus, exports to EU countries already account for 55.9 per cent (with 54.7 per cent in 2001) to Turkey – 9.3 per cent (versus 8.1 per cent in 2001), and to CEFTA countries – 5.5 per cent (versus 4.8 per cent). At the same time the share of Balkan countries goes down (from 7.2 to 6.5 per cent) and of CIS counties (from 5.8 to 4.2 per cent) in the

total export of Bulgaria. With regard to the extremely low GDP growth of European countries and reduced imports (including in inter-community trade), the reached volume of exports of over USD 3 billion in 2002 presents a considerable success. The reason lies in the widely practiced form of production under processing agreements which allows for development of trade through the use of country's competitive advantages. Turkey's recovery from the financial crisis allowed Bulgarian exports to this country to grow by 25 per cent versus the previous year. Another positive trend to be noted is accelerated growth of exports to CEFTA countries (by 24 per cent compared to 2001) which reduces the negative trade balance with this group of countries. The composition of countries that are the major consumers of Bulgarian export products is preserved: Italy, Germany, Turkey, Greece.

Total value of imports (CIF) exceeds considerably the one of exports but its 8.8 per cent growth in 2002 lags significantly behind that of exports. Following the 3.8 per cent decline registered in the first quarter versus the same period of 2001, a steady growth started and the annual value of imports in 2002 reached USD 7 806.1 m according to preliminary data (USD 7 900 m according to our estimates). Highest growth of imports was observed in the group of foods and animal and plant oils but since their share in the total import is negligible (about 5 per cent), much more important is the increase of imports of finished and semi-finished products accounting for 30 per cent, and of machinery and equipment – around 28 per cent.

The changes that occurred within a year in the commodity structure of imports lead to conclusions about the dynamics of economy development. The share of energy resources goes down (from 22.4 to less than 20 per cent) though the value of their import is maintained at a close level. At the same time, the share of raw materials and inputs remains unchanged (35 per cent) and their value goes up. Most significant are the changes in the group of investment goods the imports of which both in terms of value and relative shares is growing and accounts already for one fourth of the total import. This is a sign of a continuing growth of Bulgarian economy. The increase of consumer goods share (from 17.7 to over 19 per cent) indicates an increase of the purchasing power based demand on the Bulgarian market and intensified competition and sophistication of consumers, which exert pressure on Bulgarian manufacturers to raise their competitiveness.

The **geographic structure of imports** in 2002 confirms the growing rate of integration with EU whose share increased from 49.3 per cent in 2001 to almost 51 per cent of total imports in 2002. Highest growth is recorded with imports from Turkey – over 40 per cent. The pace of imports growth exceeds the one of exports to this country, thus resulting in reduced positive balance of bilateral trade as traditionally maintained. The import from Russia is reduced most strongly (by over 20

per cent within a year). Thus its share in total imports goes down to 14.7 per cent compared to 20 percent in 2001. Due to simultaneous shrinkage of export, the deficit of trade balance with this country remains over USD 1 billion, though decreasing versus last year.

During most of the year the deficit of the trade balance of the country registered lower levels in comparison to 2001. However, at the end of the period the deficit suddenly grew, exceeding USD 2 billion (exports FOB/imports CIF) and reaching the level of the previous year (USD 2.15 billion). This negative balance is formed mainly in two commodity groups – investment goods and energy resources where imports continue to considerably exceed exports. What is different from the previous year is that the weight of energy resources in the total deficit decreases at the expense of the weight of machinery which is related to the strive to raise efficiency of national production. A positive trend to be noted is the increasing positive balance of trade in consumer goods, as well as the decreased deficit in the trade with CEFTA and EFTA countries.

Foreign Investments

Foreign direct investments inflow in Bulgaria is strongly influenced by the slow down of world economy and the trend of decline, observed as early as 2001, continued also in 2002. Measures undertaken by the Government to encourage investments (maintenance of macro-economic and fiscal stability, reduction of profit tax and personal income tax rates, introduction of a zero rate on capital gains) proved to be absolutely insufficient to attract investors. With all the scandals concerning large privatization transactions, bureaucracy and imperfections of laws that investors keep on fighting, it is not a surprise that **the level of investments in 2002 hardly reached USD 458 m, or by USD 354.8 m less than in 2001 (revised data from BNB for 2001 show USD 812.9 m)**. This presents a drop down by more than 40 per cent. Most probably, following the usual revision 2002 data will be raised but in any case these will remain far below 2001 level. **What makes the structure of foreign investments in 2002 different from the one in 2001 is the higher level of revenues from privatization (from relatively small but larger number of transactions), higher amount of payments under inter-company loans (due to withholding of new investments by foreign partners with simultaneous repayment of previous loans) and the higher level of re-invested profit (almost 6 times).**

The ambitions of the Government and the business in Bulgaria was to encourage the inflow of foreign investments to ensure conditions for accelerated economic growth in the country. The fact that the national economy continues to register good rates of economic growth, based to a large extent on growing investment activity in industry, means that foreign direct investments present rather a supplement to local sources of

financing than major drive of growth. **Given the instability of world economy and international financial markets, the little known and not adequately regulated Bulgarian market with a relatively weak functioning system of financial mediation and justifiably criticized judicial system do not create conditions for attraction of a significant volume of foreign investments.**

In 2002 energy sector development was marked by determination to continue and accelerate reforms.

The business climate in the sector definitely improved.

Significant progress was achieved in terms of secondary legislation. In recent years the absence of such legislation made null and void certain sections of the Energy and Energy Efficiency Act. New regulations allow to proceed to a new phase of energy reforms because they set the rules of operation of energy enterprises in a liberalized environment and the conditions for those, which will continue to operate within the regulated market segment.

Defining the sector's strategic priorities, reflected in the new Energy Strategy, was a positive indication for the business circles. Endeavors to accelerate reforms and adapt the sector to market rules, where its specificity allows it, are clearly manifested in these priorities. The Strategy envisages to limit the role of the Ministry of Energy and Energy Resources to creating the conditions for the sector's development; to completely transfer the regulatory and control functions to the State Energy Regulatory Commission; and to leave the assessment of the market and its perspectives to the market itself. Thereby the recent conflict of interests between the State's functions of establishing the regulatory framework, implementing the national energy policy, regulation and control over the companies in the sector, and exercising of its rights as an owner of most of these companies is eliminated, and that is a prerequisite for development of competition and successful entry of the private business in Bulgaria's energy sector.

The firm establishment of the State Energy Regulatory Commission in the sector also contributed to improvement of the environment. Having been almost completely isolated from all processes in the energy sector for two years, in 2002 the Commission practically assumed its functions and responsibilities as a rather autonomous body.

Expectations for new legislation somewhat restrain investors' activity, despite the fact that the basic ideas of the Ministry of Energy and Energy Resources were represented to the broad public. The delay of the new energy and energy efficiency acts, which were to be adopted by the end of 2002, means a delay also in the development of the corresponding secondary legislation. This will continue to tie up the activity of quality investors in the Bulgarian energy sector.

There were not any large investments in the energy sector during the year. AES and Entergy focused their attention on the financial support of their projects for Maritza Iztok 1 CHPP and Maritza Iztok 3 CHPP, accordingly. The start of these projects is expected in 2003. Efforts for privatization of the assets in the sector were enhanced through the sale of 11 small HPPs and the start of the consultation work on privatization of the seven electricity distribution companies, which are to become private

by the end of 2003.

Expected specification of a date for decommissioning of units 3 and 4 of Kozloduy NPP and closing units 1 and 2 determined the **priority of the question about the destiny of the nuclear power plant in 2002 energy debates**. Bulgarian Government's decision to close down units 3 and 4 in 2006 is a political one and is not based on arguments about social and economic development, public opinion or the safety level of the nuclear power plant. Yet, it was the main factor which leads to **temporary closing of Chapter 14: Energy** of the negotiations for Bulgaria's accession to the EU.

The European Union laid down requirements for pre-term close down of nuclear capacities in three candidate countries - Bulgaria, Slovakia, and Lithuania. At the end of 2002 Bulgaria decommissioned units 1 and 2. Understandings on the future of the Bulgarian nuclear energy sub-sector were a major prerequisite for development of the so-called "road map" for Bulgaria, which envisaged allocation of a total of EUR 1 197 million for the country under ISPA, PHARE and SAPARD for the period 2004-2006.

Slovakia undertook to close down two units of the nuclear power plant Bohunitze, in 2006 and 2008 accordingly. These reactors are of the VVER 440/230 type and were put in operation in 1978 and 1980 accordingly. The European Council in Copenhagen took a decision to support the efforts of Slovakia to close down these units by a target aid of EUR 90 million for the period 2004-2006. Besides, EU takes into consideration that the close down of these units will be a serious fiscal burden for the country even after 2006 and will take than into account in the structuring of its follow-up financial aid.

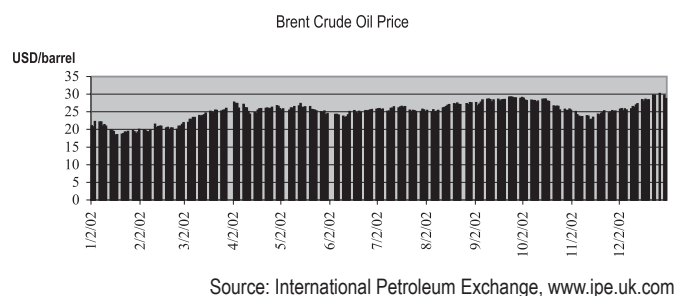
Lithuania is to close down unit 1 of Ignalina NPP before 2005, and unit 2 - by the end of 2008. The country has negotiated with EU adequate additional financial aid after 2006. The European Union has agreed that the close down of the two units will have serious financial consequences for Lithuania, because they account for around 80 per cent of total electricity production in the country. Consequently, the European Council in Copenhagen took a decision to grant to the country a target aid of USD 285 million for the period 2004-2006.

The close down of the first two units of Kozloduy NPP will not affect the capacity of the Bulgarian energy system to satisfy local market demand, because a reserve of under-utilized electricity generating capacities is available. It could lead to a slight rise of the average electricity production price in a national aspect. In itself the close down of the small units will not limit export opportunities, because the country can make use of its spare production capacity. Export problems could be generated rather by regional market demand and competition.

In 2002 crude oil price quotations at international markets were

unstable, generally revealing an upward trend. Their dynamics was dictated in the first place by the policy of OPEC, by the condition of demand and reserves in the USA, and by the escalating tension in the Middle East.

Figure 15. Crude Oil Price Dynamics



Higher oil prices had unfavorable effect on Bulgarian economy. They resulted in higher production costs for Bulgarian refineries, which purchase the raw material under conditions following international markets situation. The resulting higher oil products prices on the domestic market and international market trends lead to increased production costs of enterprises in the motor transport and the chemical industries. Given that transport serves almost all economic sectors, the effect of the higher oil prices was felt more or less by every sector.

The upward trend of crude oil prices on the international market affects with certain lag the price at which Bulgargas EAD buys natural gas from Russian and Ukrainian partners. However, a slight decrease of the price at which the company sells the raw material on the domestic market is observed. This trend is justified to some extent by the depreciation of the US dollar compared to the Bulgarian Lev, and the effect of international crude oil prices for the last nine months on the price of natural gas. Tied up prices of natural gas undoubtedly create opportunities to cut down the losses of heating companies and of the enterprises in the fertilizers and glass industries, and contributes to preservation of the competitive positions of other big natural gas consumers like the companies in the oil, cement and ceramic industries. On the other hand, artificially maintained lower prices lead to decapitalization of Bulgargas EAD and create problems for the repayment of its obligations towards suppliers, the budget, NSSI, the employees, and for the implementation of its investment program, whereby the positive effects for the economy are more or less neutralized.

In 2002 efforts to bring to normal the ratio of prices for households and non-household consumers were enhanced. SERC adopted an indicative plan for increase of electricity and heating prices in the next three years. In accordance with the plan, in the middle of the year electricity and heating prices for households increased at an average of 20 per cent and 11.4 per cent, accordingly. All other conditions

being equal, the contribution of this increase to the July inflation (compared to June) would be 1.5 per cent (but the consumer price index reflected an inflation rate of only 0.1 per cent, with the pervious month taken as a basis). At the same time, higher prices for households create prerequisites to lower the prices for the industrial sector, which will have in the long run a favorable effect on the international competitiveness of highly energy intensive productions and on national economic growth.

The structural changes in the Bulgarian transport sector developed at a slow pace in 2002. The long-expected penetration of the private initiative in the utilization and maintenance of the transport infrastructure did not happen, again. The progress in the improvement of the macroeconomic framework for the development of the transport business was insignificant.

Measures were adopted during the year that will **improve the quality of the transport infrastructure in the country in mid-term prospects**. These measures include the preparation for the construction and rehabilitation of highways sections, the construction of the second bridge over the Danube river, the modernization of Sofia Airport and Plovdiv - Svilengrad railway. The implementation of those large scale projects will benefit the business environment in the country as the transport delivers services to every sector of the economy. The new infrastructure will guarantee better connections with other foreign countries and will be a good prerequisite for attracting a bigger goods and passengers traffic.

The new railway legislation was enacted in the beginning of 2002. According to it infrastructure and transportation were separated in two companies. The separation is a necessary precondition for allowing competition in the sector. Despite the opportunities created by the legislation and the willingness declared by some private companies to operate as railway carriers, the Bulgarian Railways kept their monopoly position. The regulations allowing new entities to enter the railway transportation market were not clarified to the necessary extent and this had a negative impact on the business conditions in the sector, as well as on the business climate in the country as a whole. Even as a monopolist, the state railway carrier continued to increase its losses and could not manage to overcome the decline in the number of transported passengers and goods.

The expectations for clarifying the business conditions and the conditions for making a progress in the structural changes in the water transport remained unfulfilled. The strategy for water transport development and the amendments in the Marine Areas, In-land Waterways and Harbors Act, which had to be adopted by the end of the year according to the Program of the Government, remained only drafts. The delay in the amendments of the legislation for this sector left the issue about 23 private ports unresolved. These ports provide loading and unloading services although the existing regulation gives explicitly the right for these activities only to the public transportation ports. The ports remained in the hands of state operators despite of the willingness of the Ministry of Transport and Communications to grant concessions on them quickly, and in spite of the big interest expressed by potential investors. The successful granting of concessions over ports requires clear rules for the operation of the concessionaires. These rules had to be defined in the amendments to the Marine Areas, In-land

Waterways and Harbours Act. With a view to the good results related to the volume of processed goods in 2002 that were announced by almost all ports, even bigger investors interest in the Government's concession program may be expected, but with the lack of clear statutory regulations this interest may remain in vein.

There was no progress in granting concessions for the airports, either. The development of the air transport during the last year was marked mostly by the **problems around Balkan Airlines**, which weakened the positions of the Bulgarian aviation business on the international market. This is the reason why the Bulgarian business put a low estimate on the impact of the air transport on its competitiveness in the annual competitiveness survey at the World Economic Forum in Davos. The mark of 2.9 according to the 7-grade scale is far below the average for the world which is 4.8 and places Bulgaria on 77th position out of 80 surveyed countries, only Bangladesh, Equador and Slovakia being behind us.

During the last quarter of 2002 Balkan Airlines was declared bankrupt and the **state company Balkan Air Tour was announced the carrier under the national flag**. The main objective of that intervention was Bulgaria to remain on the international market of civil aviation services. The accomplishment of this objective is not certain yet, as the new national carrier is at the initial stage of positioning on a strongly competitive market in stagnation. Undoubtedly one of the main problems, which the company will face in the next months, is providing financial resource for its operation. The intentions of the Ministry of Transport and Communications for quick privatization of less than 50 per cent of Balkan Air Tour remained unrealized.

The past year 2002 brought about a number of amendments to the legislative framework (in some cases the planned amendments could not be completed within the year); new state and private institutions working in the high technology and communications area were established; several international seminars of very high importance were held, and at the same time the business reported unsatisfactory results (according to most of the managers of ICT companies).

Regarding the legislation and macroeconomic framework, the **following documents and statutory acts were amended or adopted** in 2002:

- The VAT Act was amended in the sense of solving the problem with VAT refund to the companies exporting software;
- Ordinance No. 13 for specifying the telecommunication activities, subject to individual licensing, registration under general license and unrestricted regime has been amended. Part of the amendments include extending the scope of activities, subject to registration under general license;
- The Corporate Income Taxation Act (CITA) was updated in its part about the depreciation rates by assets categories, and in particular: reducing the depreciation term for computers and software;
- Updated Sector Policy of the Telecommunications of the Republic of Bulgaria was adopted. The policy reflects the new obligations of the country related to the negotiations with EU on Chapter 19 : Telecommunications, the changes in the Bulgarian telecommunications market and last but not least, the abolishment of BTC monopoly;
- A Strategy for developing of e-Government in Bulgaria has been adopted;
- A draft of the Telecommunications Act has been developed;
- A draft of Bulgaria's Innovation Strategy as well as Measures for the Strategy Implementation were proposed;
- A Draft Strategy for Introducing the ICT in the High School was developed;

The efforts of the government to put the words about the priority of ICT sector into deeds and to vest the good intentions with appropriate statutory acts and administrative documents are obvious. The attempts for conducting a public debate and requesting external expert opinion on drafting laws is a good practice. Despite the update of the legislation the year cannot be defined as very successful, having in mind that part of the measures have been discussed and demanded by the business for more than two years, but some of the amendments prepared were on a quite unsatisfactory level, which lead to delays in their adoption.

The new state and business structures that were established

during the year are indicative for the increasing importance of the ICT for Bulgaria. Their objective is to create adequate environment for high technology sector development and to improve the conditions for doing business with ICT products and services on the domestic and international market. The following institutions were established during the year:

- Agency for Development of the Telecommunications and Information and Telecommunication Technology at the Ministry of Transport and Telecommunications;
- Information, Telecommunication and Management Technologies Coordination Center;
- Development of Information Technology Association;
- Telecommunications Association (ASTEL);
- Bulgarian Association for Development of Telecommunications (BADT).

This activity of business and increased attention to the sector on behalf of the state indicate that there is a will for bringing back the ICT leading role in Bulgarian industry, which could provide advantages to the whole economic development of the country by increasing the competitiveness not only of the companies from the sector, but also of the majority of Bulgarian companies in active operation.

In 2002 Bulgaria organized **a number of local and international meetings** in the ICT area that contributed to a great extent for creating the good image of the country, and at the same time, as a result of the discussions, some basic frameworks and directions for the technological development of the companies and state administration have been determined. The following are among the most important events during the past year:

- The Bulgarian Association of the Software Companies Forum;
- Regional Telecommunication Symposium for Southeastern Europe on the Development of the Reform in the Telecommunication Sector and its Impact on the Countries from South-Eastern Europe;
- The first international conference on the European Experience in the Introduction of e-Government;
- International Conference with the participation of representatives of South-East European ministries in charge of science and research.

Each of these events was followed by adoption of a document or strategy that contained specific measures and guidance for improving the condition of the sector in Bulgaria.

Besides the positive changes during the past year, some negative for Bulgaria events should be mentioned, too. One of the biggest failures of the ICT sector in 2002 was the unsuccessful attempt for privatization of the Bulgarian Telecommunications Company. Although the Government adopted a Strategy for BTC privatization as early as the beginning of the year, the deadlines of the particular stages

of the deal have been extended many times and the very procedure for selection of a potential buyer was accompanied by a number of scandals, which did not allow for the privatization of BTC and for making its future clear by the end of the year. This failure has a negative impact not only on the domestic telecommunications market, but it contributes also to the increase of foreign investors' distrust and brings harm to Bulgaria's image as a country with clear, transparent and market business principles.

At the same time the Project on Establishment of High Technology Incubators under the PHARE Program, which started as early as 2001, has been almost crucially delayed. Here the problems were related again to doubts about transparency in the project preparation stage. Of course, any delay or slowing down of such projects has a negative impact on the development of small and medium businesses in the country because it deprives the entrepreneurs of many opportunities that would have occurred if the project had developed successfully.

Number of Tourists and Revenues from Tourism

Tourism in 2002 was one of the most dynamically developing sectors of the economy. Despite the general unfavorable trends in world-wide tourism development, both the number of tourists to Bulgaria and revenues from tourism increased.

These good results are also confirmed by the data¹³ of the World Tourism Organization which indicates Bulgaria as the third most successful tourist destination in Europe in 2002 after Turkey and Croatia (revenues from tourism in Croatia in the last year amount to around USD 4 billion).

According to data from the Ministry of Economy last year the country was visited by 2 992 590 **foreign tourists**. This is by 8.6 per cent more compared to the previous year. The largest number of tourists come from EU and particularly Germany, followed by tourists from Greece and Macedonia (after deducting the so called suitcase traders). At the same time we need to note the decreased number of tourists from Russia (by 24 per cent), Ukraine (over 40 per cent), and also from Turkey. According to experts in the sector¹⁴ Bulgaria lost between USD 50 m to USD 60 m only from the introduction of visas for the citizens of Ukraine and Russia.

The number of **Bulgarians who traveled abroad** for tourism in the last year amount to 2.69 m people which is by 17.7 per cent more compared to the previous year. Most significant is the increase of the number of Bulgarians who traveled to Turkey – over 925 thousand Bulgarians preferred Turkey as tourists. Other countries most frequently visited are Greece, Macedonia, Yugoslavia and Germany.

Revenues from tourism amount to USD 1.334 billion versus revenues for the previous year of USD 1.201 billion which is an increase of over 10 per cent. **Expenses incurred by Bulgarians abroad amount to USD 615.7 m**. The balance of tourism for 2002 is USD 718.3 m versus of positive balance for the previous year of USD 632 m. These data confirm that 2002 is one of the most successful years for the Bulgarian tourist industry.

Two are **the main prerequisites for a good year in tourism** – improved quality of services and relatively low prices. The basic **problems** in tourism, as pointed out many times, remain valid – poor quality of infrastructure (mainly the transport one), lack of adequate promotion policy and established specific image, and a reserved trade mark of Bulgaria as a tourist destination; lack of sufficient sport, cultural and other entertainment events for tourists, etc.

Another serious problem of Bulgarian tourism is its monocultural nature (domination of sea side tourism), as well as the circumstance that it is oriented to a considerable extent to poorer and older tourists. It needs to shift its orientation towards richer customers and to combine better sea side and alternative tourism up the country.

Alternative tourism in Bulgaria is developed increasingly successfully. According to data from BAAT in 2002 about 3 500 fans of alternative and rural tourism in particular visited the country and spent around EUR 0.5 m. According to data from the association Bulgaria has the potential to receive around 140 000 people a year in alternative forms of tourism.

Good opportunities are also offered by **eco-tourism**. In 2003 PHARE will fund eco-tourism development projects at the amount of approximately EUR 7 m. and the same amount is expected to be invested in cultural tourism.

Last year about USD 280 m¹⁵ were invested in specialized tourist infrastructure which is a guarantee for its future modernization.

Regulatory Framework

Work continues on the development of a **National Strategy for Development of Tourism**. In the course of drafting is also a **National Strategy for Development of Eco-tourism**. It is expected to be completed in 2003. Representatives of the ministries of economy, the environment and agriculture are involved in its elaboration. The aim is to make the country a leading destination for alternative tourism among Southeast European countries and to encourage development of European trans-national eco-tourist routes.

As of 1 October 2002 the **new Tourism Act** entered into effect. It regulates in detail the relations between tourists and tour operators or agents. The Act alleviates the licensing regime by repealing licenses for restaurant and hotel running but keeping the ones for tour operator and tour agency activities. The Act outlines also the role of local governments in the control and development of tourism on local level.

Several **regulations to the Act** became effective, too – the Ordinance on Categorization of Tourists Sites, the Ordinance on Licensing of Tour Operators and Tour Agents, as well as the Tariff of Charges collected under the Tourism Act. The requirements for categorization of tourist sites are raised.

As of 1 January 2003 tour operators must also offer insurance contracts under another regulation to the law. Businesses will pay 7 per cent VAT on tourist services.

At the end of last year an **Executive Agency for National Tourism Promotion and Information** was established as a legal entity funded from the national budget. This agency is going to implement the National Promotion Program. It will set up and maintain a national electronic system for tourist information. Thus, it is expected that one of the basic problems of Bulgarian tourism will be solved – the lack of well organized and attractive promotion of the country.

¹³ Presented at the Second International Conference on Tourism Bulgaria – Dreamland held in Sofia, 9-11 Jan., 2003

¹⁴ PARI daily, 6 Jan., 2003

¹⁵ PARI daily, again, 6 Jan., 2003

The general macroeconomic stabilization of the country in 2002 and the start of negotiations with EU on Chapter Agriculture created favorable preconditions for restructuring of a number of agrarian sub-sectors on the way towards successful completion of the transition to market relations. At the same time, problems generated by overfragmentation of farm land and limited access to loans, which have direct effect on the quality of agrarian output and hence on its positions at international markets, remain outstanding. The share of agriculture in GDP preserves a downward trend, but remains rather large - around 11-12 per cent. Estimated number of employed in this sector exceeds 25 per cent of Bulgaria's economically active population.

In 2002 the Government's agrarian policy followed the priorities set forth in the **2000-2006 National Agriculture and Rural Development Plan and the 2001-2005 Government Program for Development of the Agrarian Sector**. Throughout the year Government-implemented measures were generally aimed at creating conditions for more efficient management of land resources, development of market structures, increasing the level of competitiveness (both of agriculture and of the food industry), promoting the export orientation of the agrarian sector, and gradual implementation of the components of EU's Common Agricultural Policy.

With the **start of negotiations on Chapter Agriculture in March 2002** and in fulfillment of the task for their acceleration and completion in December 2003, the work on harmonization of legislation in the field of agriculture was intensified. Approved amendments to the Farmers Support Act, which regulates government support to farmers, and the implemented measures incorporated in the National Agriculture and Rural Development Plan are of paramount importance. The act sets forth as major fiscal instruments direct subsidies, including current, investment and export ones, long-term lending under three investment programs, and intervention on the farm products market. Outlined priorities include the grains sector, stock-breeding, perennial plants, and vegetable-growing.

The functions of the Agriculture Fund were approved: to provide financial support to farmers; to intervene on the markets of farm products; to grant export subsidies; and to perform the management of the SAPARD Program. The passed Act on the Census of Bulgarian Farms, which sets forth 1 July 2003 as a starting date of the census, is of paramount importance for the process of negotiations on Chapter Agriculture. The amount, scope, and orientation of direct subsidies and payments in the agrarian sector, to be allocated for Bulgaria following its accession to the EU, will be dependable on that.

Amendments to the Ownership and Use of Farm Land Act and the Regulation on the Terms and Procedure of Fixing Current Market Prices of Farm Land were introduced with a

view to overcome a major weak point of Bulgarian agriculture - farms fragmentation and the absence of a normally operating land market. The Government also approved amendments to the Stock-breeding Act, which are related to both the need to consolidate farms and set up modern farms having capacity to produce quality commodities, and the development of stock-breeding in compliance with environmental standards. **A regulation on the Terms and Procedure of Planting New Vines, Transplanting, Engrafting and Uprooting Existing Vines** was passed with a view to support and regulate wine production. Implemented measures in the field of veterinary and phyto-sanitary inspection allowed to finalize negotiations in this area of European legislation as early as the beginning of December 2002, that is, only nine months after their start.

Alongside with the further harmonization of the legislation, the ongoing liberalization of trade in agricultural products between Bulgaria and the EU, and the licensing of Bulgarian producers for exports to the EU, another topical matter is the establishing of the required institutions and administrative structures for application and control over the compliance with the newly adopted legislation, the restructuring and refurbishment of veterinary and phyto-sanitary laboratories and border control points, as well as the development of agro-statistics in compliance with the EU requirements.

Significant role in the setting up of a competitive agricultural sector is assigned to the **SAPARD pre-accession EU program**, under which Bulgaria receives Euro 53 million per year. Amendments to Ordinance No. 14 regulate the terms and procedures of providing grant aids to farm producers to invest in farms under SAPARD. As at year end the funds utilized under the program amounted to more than BGN 30 million; they were spent for the implementation of 118 projects, which were completely finalized by that time. Approval has been granted by now to 298 projects amounting to a total value of BGN 200 million. Amendments to the application procedure were introduced during the implementation of SAPARD, with a view to facilitate applicants. In the first place, candidates have been granted 10 days to correct the technical errors of project dossiers. Second, it was agreed with the European Commission to organize the sessions of the Commission for Approval of Projects under SAPARD on a monthly basis. Third, a start was given to the set up of special regional recipient agencies to process applicants' documents. Accumulating experience in project development, submission and approval is expected to accelerate the process and contribute to the utilization of allocated funds.

The export orientation of the sector is confirmed by the high growth rates of export of agricultural products and foods, and by the positive foreign trade balance of this commodity group. Government-implemented measures to intervene on the grains market, to set up a wheat commodity fund and to subsidize export-oriented grain producers proved effective (though

temporarily) and contributed for certain revival of the grain market. On the other hand, the decision to intervene, taken as an emergency case, brings up the issue of the absence of clear and comprehensive concept of the sector's operation and the role of Government on the agricultural commodities market. The seasonal duty charges on the import of eight vegetables used by the processing industry, introduced in mid August in protection of local producers, generated similar reactions. Thereby applied custom duties were adjusted to WTO's bound rates. Subsequent debates revealed the need of continuous profound analysis of the market situation, with a view to establish the real cause of market shocks and enable the Government to take adequate trade policy measures to regulate the market.

Several positive trends were observed on the capital market in 2002: the start of the trading of compensatory instruments, the increase of the SOFIX index, and the market capitalization increase.

However, **the capital market's role in Bulgaria's financial sector remains insignificant** – as of the end of December 2002 the total market capitalization of the Bulgarian Stock Exchange – Sofia AD was a little over 4 per cent of the updated estimate (as per the Ministry of Finance assessment) of the 2002 GDP. This is explained both with the condition and prospects of the Bulgarian economy as a whole, and the attractiveness, and even availability of projects, which would find financing through this alternative non-banking environment. At the same time the potential of the capital market as a source of funding remains unknown or not-preferred even in the cases when relevant projects are in place. As a result of these and other factors liquidity remains low, the market does not promote the good corporate governance practices, and the investment alternatives remain limited. Financial brokerage continues to be carried out mostly through the banking sector.

The first quarter of the year marked a decline in some of the main market indicators, which characterize the capital market condition in Bulgaria (which is understood and measured traditionally by means of the indicators of the Bulgarian Stock Exchange AD). Among the significant corporate news in the **second quarter** were the annual financial statements of some of the most traded companies, which were published at the end of March and the beginning of April. The expectation for dividends and the forthcoming dates of the annual General Meetings of the Shareholders were the two main factors stirring the fluctuations in the prices of the shares with better liquidity. The General Meetings, however, did not in all cases meet the expectations of the portfolio investors. Nevertheless, the dependence of the prices of the traded companies on the publicly announced corporate events remained contradictory. In addition to this problem it may be said also that the accounting and regulatory practices and corporate governance principles need further upgrading.

With the exception of the index, the **third quarter** did not mark any positive fluctuation of the market indicators. Liquidity remained a major problem in stocks trading. The third quarter, however, manifested a higher liquidity of some of the securities included in the calculation of the SOFIX index, which was undoubtedly a positive development. The **last quarter of 2002** was definitely positive. The serious shortcomings of the capital market, however, remained in existence. The increased turnover in the last month of the year was due partially to transactions aiming solely and only to achieve a certain taxation effect. Although some liquid positions marked a considerable growth in prices in the last quarter and attracted the investors' attention, they are not included in the SOFIX index. The latter fact challenged again the capacity of the SOFIX index to reflect

the market condition adequately.

The summary of still other events in 2002 leads to indicative conclusions about the condition and prospects of this market in Bulgaria. In July 2002 the Council of Ministers adopted **an annual list of 1,073 companies** with state ownership shares of which could be sold (by means of various privatization methods, including public offering through the Stock Exchange) against compensatory instruments and investment bonds. Alongside with that some bylaws were also adopted for regulation of the issuance and transactions with compensatory instruments. The expectations from these measures specifically for the development of the capital market boiled down to two aspects. First, the new regulation of transactions with compensatory instruments and mostly the concentration of the trade on the Bulgarian Stock Exchange AD would result in better transparency and clarity in pricing, improved liquidity and thus indirectly, to recovering confidence in securities trading and the capital market as a whole. Second, the sale of new blocks through the stock exchange by the state, even against non-cash means of payment, would raise the trust in the privatization process and the direct interest in the stock exchange.

The start of the trade in compensatory instruments on the floor of the Bulgarian Stock Exchange - Sofia AD was undoubtedly among the leading events on the capital market throughout the year 2002. At the end of August the Board of Directors of the Bulgarian Stock Exchange - Sofia AD passed a resolution for registration of the compensatory instruments (on the Non-Official Market, Compensatory Instruments Market Sector). The trade started in the three issues of bonds, which comprise the group of compensatory instruments in compliance with Compensatory Instruments Transactions Act.

While compensatory instruments trade was lively and recovered the interest in the potential of the organized capital market, particularly the lack of clarity specifically regarding **the exchange privatization** cast doubts on the prospects, at least in the mid-term run, of fostering the capital market in Bulgaria.

The adoption in July of the annual list of companies for privatization against non-cash means of payment did not allow making firm forecasts regarding the emergence of new companies to be traded on the Bulgarian Stock Exchange - Sofia AD. The two main reasons for the latter were: First, the procedure for making those companies public was obviously going to take a long time. Second, there still existed concerns about further changes in the list of companies for privatization against compensatory instruments and investment bonds (including the part of companies on the list for privatization through the exchange).

These concerns prove out justified for the time being. At the end of September the Privatization Agency passed a decision

determining public offering as a method for the privatization of 85 companies (mostly minority blocks of their shares). It was envisaged that these companies would be grouped and sold in pools. This fact actually constituted a reduction of the initial list for privatization through the exchange and therefore the financial community received it with disappointment. Afterwards, for various reasons, some pools were taken off the list of the 85 companies, and this caused uncertainty in the expectations from the stock-exchange privatization. Especially negative response came from the owners of compensatory instruments.

At the end of the year the Privatization Agency reported that procedures had been initiated for 11 pools of minority blocks of shares of approximately 90 companies, which will be traded against compensatory instruments. Investment intermediaries were selected for 5 of them, and again at the end of the year shares of 17 companies were registered on the floor of the Bulgarian Stock Exchange - Sofia AD. Regretfully, in the beginning of 2003 the marketing of the first pools for privatization showed that another problem existed, too: there were cases when the intermediaries were the successful bidders at the Privatization Agency tender and undertook an obligation for a high minimum sale price, while afterwards they failed to sell at this price and the sale was considerably delayed¹⁶.

The capital market fostering in Bulgaria in 2002 by the means of the government policy remained questionable also due to the lack of clarity about the privatization through the stock-exchange. The foregoing conclusion is confirmed for example by the fact that practically all deadlines in the **Government's Program for Development and Fostering of the Capital Market in Bulgaria**, which was distributed in March 2002, were not met.

In the beginning of 2003 the **new Accountancy Act** entered into force; it stipulates that the mandatory application of the International Accounting Standards will be introduced in the beginning of 2005, and it will be in force from the beginning of 2003 only for banks, insurance and investment companies, issuers pursuant to the Securities Public Offering Act (and others that operate in compliance with specialized laws). According to the new taxation regime applicable since the beginning of 2002 one of the tax incentives has become the cancellation of the tax on capital gain from certain transactions with securities in the case of juridical and natural persons.

A positive step and a manifestation of the government policy can be considered to be the **adoption of the Act on Amendments to the Securities Public Offering Act**, which was subjected to long discussions and promulgated at the end of June. The amendments to this Act were necessitated mostly by the need to adjust the imperfections in the Securities Public Offering Act passed at the end of 1999, and also they were necessary with a

view to filling the gaps in the regulatory framework, which were noted in the course of application of this Act.

The amendments were targeted at strengthening the confidence in the capital market, protection of the rights of minority shareholders and investors, raising the powers of the State Securities Commission and development of corporate governance. With the new provisions of the Securities Public Offering Act a substantial change was caused in a number of areas having to do with the market operation and development – for example, areas like capital increase and decrease, offering through bidding, disclosure of information, public companies management and the public nature as such.

Concerning the statutory framework, 2002 brought about a development relating to the **Companies with Special Investment Purpose Act and the Financial Supervision Commission Act**.

The first draft was passed at first reading on 1 October 2002. The hope is that it will make a serious breakthrough in the environment for the capital market development in Bulgaria – both in connection with the possibility for emergence of such companies with special investment purpose, and more generally, with the introduction of landmark norms in Bulgaria about assets securitization. The creating of alternatives and the encouragement of joint investment schemes are mentioned as additional grounds for the draft. Discussions are still underway.

The draft of the Financial Supervision Commission Act was adopted also at second reading in the beginning of December. The draft concerns the unification of the supervision over the non-banking financial sector in Bulgaria: capital market, insurance and social security of the fully funded type. The costs reduction, the reduction of the existing administrative staff and the efficiency improvement are the major grounds behind the idea for integrating the supervision. Meanwhile there were intensive discussions both on the very essence of the idea for a unified supervisory body, and on removing the existing shortcomings of the draft law of legal and technical nature, which would possibly be an impediment to the current regulatory and supervision practice or the future establishing of the new supervision regime.

By President's Decree the adopted Act was returned for reconsideration. The President challenged the draft-provision that the decisions of the Financial Supervision Commission would not be subject of appeal in court, and he also challenged some of the provisions regarding the annual fee, which the persons subject to supervision will have to pay to the uniform financial regulator. The draft law was passed again by the Parliament in

¹⁶ See the interview for the *Pari* newspaper with L. Lekov, analyst at the Investor.bg.: *The Lessons from the Failure with the Zlatni Pyassatsi Pool*, 7 February 2003.

January without any changes.

The improvement of the legal framework and the other manifestations of the government policy are traditionally present in the review of the capital market in Bulgaria. One of the reasons for the above is the lasting inability of this market in Bulgaria to overgrow the initial stage of development and to become a real alternative of banking brokerage or a medium for enhancement of investments. The conclusion is that **alongside with the objective state of the capital market (according to the trade on the Bulgarian Stock Exchange – Sofia AD) the review of the environment for development and the Government policy as such also gives rise to contradictory assessments.**

The banking system dominates Bulgaria's financial sector. The condition of banks in Bulgaria remains stable; they have excellent capital adequacy and liquidity indicators accompanied by a well-functioning banking supervision. At the same time, however, the banking system is still relatively small in terms of both assets and loans share of the GDP. As of the end of December 2002 there were 34 banks in Bulgaria; 27 of them are banks licensed to operate in Bulgaria and abroad, one bank has a license to operate in Bulgaria only, and there are six branches of foreign banks. In the last quarter of 2002 the number of banks decreased after the actual merger of HVB Bulgaria with TB Biochim.

According to BNB data, as of the end of December 2002 the banking system had assets amounting to BGN 14,557,124,000. At the end of December the deposits totaled BGN 11,282,160,000. The current profit of the banking system in December was BGN 266,625,000, while in September it was BGN 201,740,000, and in June 2002 it was BGN 132,715,000. In the last month of 2001, however, the current profit of the banking system was BGN 319,375,000. According to data from the BNB the capital adequacy of the commercial banks as of the end of September 2002 was totally 26.84 (group five excluded). At the end of September 2002 the primary liquidity for the banking system as a whole was 9.03 per cent, and the secondary liquidity was 26.88 per cent (at the end of 2001 these indicators were 13.47 and 25.47 per cent respectively).

Thus the banking system as a whole continued to increase its assets and deposits, as well as its current profit throughout 2002. The banking system current profit in December was still smaller than that in the last month of 2001, the explanation being to large extent the accounting and reporting of costs for provisions for losses from lending; therefore this indicator does not give direct information about the system development. On the other hand, however, the ratio of net income from interest to other non-interest revenues decreased inconsiderably (from 2.30 to 2.25 at the end of 2001 and 2002 respectively, while at the end of 2000 it was 2.18), which indicates underdevelopment and insufficient diversification of banking activities. The capital adequacy indicators as of the end of September were lower compared to both the end of June 2002 and the end of 2001; nevertheless, they are relatively high and are an evidence of the system stability. The banking system liquidity indicators in total for September show multifold fluctuations after the end of 2001 (the primary liquidity ratio was decreasing, but that of secondary liquidity was increasing), but they are still relatively high. All the aforesaid can be interpreted as an indication that **stability is in place in Bulgaria's banking system, but the short-term trends were contradictory, and the banking system remained not quite efficient, and underdeveloped.** The latter conclusion can be confirmed to a certain extent also by the banks' lending activities review.

Given the absence of many of the products and services offered by similar institutions in the West, as well as due to the financial sector condition in general, the analyses of the Bulgarian banking system are still being limited to two groups of issues: lending and property restructuring.

Further on, amendments to the statutory regulations, aimed at **enhancing bank lending**, entered into force in the beginning of 2002. For example, the amendments to the Corporate Income Taxation Act for 2002 exempted the interests on bank loans from the weak capitalization regulation. Amendments to the Penal Code repealed the criminal liability of bank managers responsible for granting certain credits.

Lending to the non-governmental sector showed a clear trend of increase throughout the year (under the Currency Board regime this is lending from commercial banks, which includes lending to non-financial state-owned companies, private enterprises, households and non-banking financial companies). From BGN 4,374,627,000 at the end of 2001 the receivables from loans to the non-government sector reached BGN 6,250,741,000 at the end of December 2002. The newly agreed loans from commercial banks in 2002 amounted to a total of BGN 5,189.7 million, while in 2001 the newly agreed loans were totally BGN 3,084.21 million (growth of 68.27 per cent).

The quality of the lending portfolio was also improving: at the end of 2001 92.98 per cent of all categories of loans in the banking system were performing, then at the end of June 2002 93.87 per cent were performing, and at the end of September 2002 – 94.44 per cent. This general conclusion holds true also particularly for the receivables from loans to private enterprises and households. Perhaps with the exception of receivables from enterprises under long-term loans in Bulgarian levs, the percentage of performing loans compared to the respective group of loans was either increasing, or remained high in 2002.

The interest rates on short-term and long-term lending in Bulgarian Levs dropped in December 2002 as compared to the end of 2001, this being more strongly manifested with short-term lending.

With the development of the economy and the emergence of concrete projects, alongside with the expansion of competition and efficiency in the banking sector itself, an increase of the long-term lending to the private sector may be expected. Further on, the increase of lending to households in 2002 is only one of the indications of the further development of retail banking, which we have been witnessing recently. Despite the objective indications of a trend towards increased lending activity, at present there prevails the assessment that lending from banks to companies is still low, including that to small and medium-size enterprises.

The analysis of the Bulgarian banking system should take into account also **ownership restructuring**, which has been taking place in the recent years. Through various channels, such as privatization, opening of representation offices, branches and newly established banks, the foreign participation in Bulgaria's banking system is already prevailing both in the equity control and managed assets. According to data quoted by the BNB¹⁷, private banks account for 79.6 per cent of the total banking system assets as of the middle of 2002. At that same time foreign banks and investors controlled 72 per cent of the banking assets.

In the last months of 2002 significant development was observed regarding the privatization of the last two large state-owned banks, and the leading role here again belonged to the foreign investors and consultants. TB Biochim privatization and HVB Bulgaria acquisition were completed by the end of 2002. After the privatization of TB Biochim, private banks in Bulgaria account for almost 85 per cent, and foreign banks and investors for almost 77 per cent of the total assets in the banking system (according to data of mid-2002).

The last large state-owned bank is DSK Bank AD (State Savings Bank); the latter, together with the Encouragement Bank, account for the remaining 13.4 per cent of the state share of banking assets. In mid-December 2002 it was known that five potential buyers had shown interest in DSK Bank. The deadline for submitting indicative bids by the applicant-buyers expired at the end of January 2003. Bids were submitted in due time by: the Austrian Erstebank, the Hungarian OTP, and the Greek Pireus Bank.

Another interesting fact, which is indicative of the trends and prospects for development of the Bulgarian banking system, is the proposal placed in April 2002 by the Commercial Banks Association suggesting that **banks should be allowed to sell insurance and social insurance products based on commission principle**. According to the justification provided by the commercial banks representatives, in this way the basic banking activities will be expanded and assisted, but without change in the extent of the risks assumed insofar as such transactions will be implemented on behalf and for the account of the insurer or employer paying the social security contributions. Such a decision would be in line with the universal nature of the Bulgarian banking system, however, the regulatory aspects relating to the reasonable banking activities and consumer protection will have to be carefully assessed.

In 2002 there were **also amendments to the laws and the related statutory regulations**. The **two drafts for amendments to the Banking Act**, which were submitted in March 2002, **were passed in July**. The first one strongly reduced the requirements to the type of education of bank

managers. According to the justification submitted by the proponent the proposal is in line with the policy for banking sector liberalization by repealing some unnecessary restrictions on the conducting of banking activities. Repealing of some of the previously existing limitations gave rise to a lot of discussions, but it became a fact after the amendments to the Banking Act were promulgated in the Official Gazette.

The second draft law was aimed at granting expanded powers to the BNB to control the off-shore shareholders of banks, holding 3 per cent or more of the voting shares. This draft was justified with the need of strengthening the banking supervision, ensuring transparency in the shareholding structure and compliance with international regulatory standards.

In December 2002 a group of MPs from the ruling coalition put forward to the Parliament **a new draft for amendments to the Banking Act**. The single proposal in this draft was a requirement to be put in place that at least one Bulgarian citizen should be elected a member of the managing bodies of a bank, and this member should be required to speak Bulgarian language and to have lived in Bulgaria for at least one year preceding his/her election. The draft is justified by the need of better communication between commercial banks and official Bulgarian institutions, easier adaptation to the Bulgarian market and better knowledge of the situation in the country. This justification stems from the concern of certain representatives of the banking circles in Bulgaria regarding the restricted access of Bulgarian bankers to senior management positions in banks, most of which are already under foreign control. The draft is being considered.

A draft on Amendments to the Bank Deposits Insurance Act was also adopted in December. **The secured amount of deposits in banks was raised from BGN 10,000 to BGN 15,000**. The main grounds for such an increase was to achieve better compliance with the European directives and Bulgaria's commitment to have the depositors' security reach Euro 20,000 at the time of the country's accession to the European Union.

In September 2002 the **Bank Insolvency Act** was promulgated. The delay in passing this Act was among the problems identified during the review of the latest agreement with the IMF. The draft was put forward as early as the end of September 2001. Pursuant to this new Act the administration of banks insolvency proceedings should be assigned to the Bank Deposits Insurance Fund. New control was introduced also over the activities of trustees in bankruptcy, and the responsibilities for such control were assigned again to the Bank Deposits Insurance Fund.

A draft on Amendments to the Bulgarian National Bank Act was put forward to the Parliament in June. The main proposal in this draft was that BNB branches in the country and abroad should be opened and closed down only after the approval of

¹⁷ Source: BNB report on the first half of 2002

the Parliament. It was suggested also the BNB branches to be allowed to sell and buy government securities. In July a second draft on Amendments to the BNB Act was submitted. The latter suggested that the BNB headquarters and branches should be explicitly specified in the Act.

Both above-mentioned draft laws were underpinned by the willingness to oppose the decision made by the BNB to close down three of the regional branches: Rousse, Bourgas, and Vratsa. Although the BNB Managing Board had made a decision to that effect back in 2001, at the end of October 2002 the deadline for the closing-down was coming closer and this aroused dissatisfaction among those concerned and resulted in the above draft laws and in strong public response of the concerned employees in some of those regional branches. Representatives of the BNB itself strongly opposed such ideas¹⁸. On one hand, they justified their decision with the need of optimization of the regional structure and general improvement of the BNB efficiency. On the other hand, the BNB perceived that response also as an encroachment on the independence of the Central Bank of Bulgaria.

The two draft laws for Amendments to the BNB Act, submitted in June and July respectively, were not adopted in the end. However, the topic about the regional branches was one of the most widely discussed in the media in the summer of 2002, and ultimately the strong pressure resulted in a trade-off decision by the BNB: in the beginning of September the Managing Board of the BNB passed a resolution, wherein it partially revised its previous position – the regional branch in Vratsa was closed down, and the regional branches in Bourgas and Rousse were transformed into BNB representation offices, with no desk operations.

In 2002 the **new Ordinance No. 3 of the BNB regarding Paperless Entries and the National Payment System** was promulgated and entered into force. Actually this was the latest step preceding the introduction of the new payment system of real-time gross settlement. The new system will allow for prompt processing of payments within a few seconds. Each bank will be able to monitor continuously the movement of funds in its accounts and to respond in case the liquidity drop down. After it is commissioned, all payments of system importance will go through it. The system is expected to be completely set up within one year. It is planned that the client payments, which do not need to be effected in real time, will be left for servicing to BankServcie.

In the last quarter of 2002 **amendments were made also to some bylaws**. Some of the more important ones are the following instruments issued by the BNB: newly issued Ordinance No. 9 (which substituted the one of 1997) for assessment and classification of the bank risk exposures and formation of provisions for losses due to devaluation; new Ordinance No. 5 (replacing the previous one of 1998) on the

order and conditions for acquisition of, payment and trading in government securities; as well as Ordinance No. 15 on control over transactions with dematerialized government securities.

¹⁸ Ref. Interview of Sv. Karaneshev, Director General of Issue Division, before Econ.bg, dated 17 July, to be found at <http://www.econ.bg/advises.html?type=3&lang=1&id=5126>

The year 2002 can be defined as a year of transition in the social policy of Bulgaria and a strive towards better coordination between economic and social policies for the future. The Government announced for the first time strategic goals and intentions and the first practical steps in this direction were made. The new approach in the social policy suggests mandatory accounting for the social effects from the introduction of all economic measures, an active and preventive social policy, application of a differentiated approach and consistent fiscal decentralization in the social area.

Two key areas in the focus of Government's attention are the policy on the labor market and social assistance. In 2002 specialized employment programs were developed and tested and amendments were introduced in the regulatory framework of social assistance. Implementation of these measures will continue in 2003, funding being ensured from the national budget. Compared to 2002 the funds for social expenditures and reduction of unemployment are increased by nearly BGN 900 m. The relative share of social expenditures in the 2003 budget amounts to 38 per cent of total non-interest payments, or about 14 per cent of GDP.

Apparently, the year 2002 can be defined as more socially oriented as far as Government's policy is concerned. The simultaneous application of measures to encourage both demand and supply will require good balancing and coordination of economic and social policies. Subsidized employment is successful as a temporary measure to tackle with unemployment but it should be accompanied by a policy to encourage opening of permanent and efficient jobs.

Social Security

A major emphasis in **the area of social security** in 2002 was placed on the draft of the Ministry of Labor and Social Policy and the National Social Security Institute of a new Social Code seeking ways to increase the collection rate of social insurance contributions, in order to solve the continuously growing deficit of the Pensions Fund and to create conditions for fair competition of businesses with regard to the labor market, to protect bona fide employees and employers and to achieve social justice.

The **minimum social insurance thresholds** by economic activities and groups of professions as of 2003 for employees under labor contracts and under company management and control contracts were introduced not in an administrative way but as a result of negotiations between employers and trade unions, aimed at encouraging social dialogue between the Government, trade unions and employers and at assessing the actual condition of labor demand and supply on the labor market. Thus, in reality two thirds of the minimum social insurance threshold were negotiated between employers' and trade union organizations and the remaining one third

was determined through an expert evaluation, again with the involvement of representatives of employers, trade unions and the Government. These will be in effect until the end of 2003 and then will be negotiated again. In October the European Commission recommended that wage negotiations in Bulgaria should be held only between employers and trade unions, without the involvement of the Government which currently determines the minimum wage level. This was written down in the joint report on evaluation of labor market priorities presented by the Bulgarian Minister of Labor and Social Policy and the Commissioner for employment and social issues at EC. In this respect, negotiations are expected to start in 2003 for determining minimum wage levels by industries and occupations.

The Bulgarian Industrial Association openly declared their dissatisfaction with the postponed introduction of social legislation amendments promised by the social ministry as of 2003 and employers are expected to incur a damage of about BGN 194 m. The still low income of citizens, the high unemployment rate in the country, the high number of people in need for social protection, and overall inefficiently functioning labor market are the reasons for postponing equalization of the insurance burden between employers and the insured by two years.

Mandatory registration of labor contracts with NSSI as of 2003 is the second measure undertaken by the social ministry to prevent payment of non-regulated remuneration resulting in evasion of taxes and social insurance contributions. Overall, employers welcome Government's measures to curb gray economy in the country, which amounts to 25-30 per cent according to experts, but they think time limits are irrational and unacceptable, and financial sanctions do not match reality.

The new measures included in the Social Code are envisaged to bring additional revenues to the budget of social insurance at the amount of BGN 162 m, but only time will show whether the forecasts of NSSI experts will come true.

At the end of November the deadline expired for recruiting the minimum number of 15 000 insured persons for Occupational Pension Funds, so that they can continue to operate. Occupational Pension Funds and in particular five of them (Occupational Funds Rodina, ING, LUKoil Garant, Nuton Sila and Bulgarian Pension Insurance Company) hoped this requirement will drop down with **the amendments to the Social Security Code**, unfortunately it was not passed at second reading in parliament. The amendment that envisaged extension of the period for one more year also reached only first reading. The law has still not regulated transfer of insured persons from one fund into another to allow choosing between desired risk and return on invested funds of the insured.

Ordinance N 4 of the Ministry of Finance was published in

the middle of the year which stipulates **the limitations of investments abroad of the assets of pension insurance companies and funds for supplementary pension insurance**. It recommends that funds of the insured be invested in securities traded on regulated markets of countries with which Bulgaria has signed agreements for encouragement and mutual protection of investments. The purpose is to protect to a higher extent the funds of the insured and to encourage their participation in supplementary voluntary pension insurance.

The association of companies for supplementary pension insurance had a negative attitude towards some texts of the draft of the new Social Code concerning investment regime of companies, increased powers of the State Insurance Supervision Agency, securitization of required minimum return on investment of the funds of the insured with company's own funds, the requirement that only one custodian bank may keep the funds of a pension fund and the envisaged increase of the minimum equity of companies to ensure financial stability. The changes proposed by the social ministry concerning investment of assets of pension companies indicate that private pension funds will continue to be subjected to a strong control by the government.

At the end of 2003 according to NSSI data pension funds are expected to manage over half a billion levs. At the end of 2002 this resource amounts to BGN 340 m, out of which almost BGN 150 m belonging to the funds for supplementary mandatory insurance and the rest – to voluntary funds. NSSI experts are of the categorical opinion that the effect for the Universal Funds of the introduction of minimum social insurance thresholds by economic activities and groups of professions will be minimum. The reason lies in the fact that it is mainly young people who are insured in Universal Funds and they have low incomes and short length of service. No great effect is envisaged for Occupational Funds, too, because there are almost no individuals on minimum wage among the insured in these funds. The effect of the thresholds is expected to be felt mostly on the level of state social insurance, i.e. the first pillar of the pension system in Bulgaria.

Employment and Unemployment. Labor Market Policy.

With regard to the indicator **number of registered unemployed** 2002 is definitely a positive year. The unemployment rate in Bulgaria dropped down from 18.57 per cent in January to 16.27 per cent at the end of the year. According to EUROSTAT data at the beginning of 2002 Bulgaria has highest unemployment rate among candidate countries while for the six months it follows Poland and Slovakia.

The expired 2002 is a combination of attenuating pace of restructuring and liquidation of loss-generating enterprises (of which it could be stated that the peaks are overcome) and large-scale intervention of the government to cut down

unemployment by opening subsidized jobs.

Despite the relatively positive changes **significant regional discrepancies and high unemployment rate in rural and ethnically mixed areas** are still concerning. Problem groups of unemployed are people of advanced age, Roma, long-term unemployed and disabled people. At the same time they are the ones of lowest education and qualification level and low mobility on the labor market. These people experience great difficulties in finding a job and rely exclusively on social assistance. In addition, most of them are people of working age but due to the mismatch between demand and supply of labor they remain permanently out of the labor market.

In response to those specific structural characteristics of unemployment in Bulgaria, in 2002 the Ministry of Labor and Social Policy developed and applied **a number of active measures on the labor market** with the aim to cover the unemployed of working age in hardest social position in various forms of subsidized employment.

The program for micro-crediting through the so called Guarantee Micro-credit Fund planned for BGN 20 m in 2002 out of which BGN 14 m were appropriated. 1400 projects were approved which are to provide over 3000 new jobs.

Incomes and Living Standards

According to the statistics of household budgets **an increase of nominal incomes of Bulgarians** was registered in 2002 both from wages and social payments. This results from the economic growth and placing unemployment problems in the focus of Government's social policy. Though unevenly in the different quarters and accounting for inflation, compared to last year real incomes have generally increased.

From the view point of structure of general household expenses in 2002 the share of food expenses remains traditionally high. At the same time last year prices of non-food goods and services increased considerably resulting in general increase of household expenses for electricity, telephone, water supply and house maintenance. In this context, extremely acute is the issue of further restructuring and privatization of infrastructure sectors and their social affordability with regard to their impact on prices and household expenses.

The overall positive trends of incomes are reflected in the results of regular surveys on "consumers' confidence" carried out by the National Statistics Institute. The expired year started with extremely pessimistic assessment of the present and expectations of the future financial condition of households, inflation and unemployment. However, after October 2002 the trend changed and consumers' expectations are more optimistic.

Social Assistance

(unemployment and poverty among Roma, problems with tobacco buy-out and other agricultural products among Turks).

The expired year 2002 is characterized with **important changes in the area of social assistance**. Generally, these boil down to more efficient channeling of funds exactly to those social groups which mostly need them. It is worth noting in this respect the adoption of the Act on Family Allowances for Children and the amendments to the Social Assistance Act and its regulations. On the basis of specific coefficients increase of social assistance is guaranteed for the most vulnerable social groups. The second positive element is the attempt to reach better coordination between the policies of the labor market and social assistance and the manner of assisting people of working age. Instead of social aid some of them will receive remuneration for work and guaranteed access to training and qualification programs.

Social Partnership and Industrial Relations

Overall, 2002 passed under the conditions of active social dialogue and cooperation, regardless of the occurrence of conflict areas and aggravated relations at times between employers, trade unions and the government. Two important documents were adopted on national level – **the Charter for Social Cooperation and the Cooperation Agreement between the Council of Ministers of the Republic of Bulgaria and Representative Organizations of Employees and Employers**. From this perspective Bulgaria fully meets European norms and requirements.

On the level of enterprises, the **first workers' councils were set up as an experiment in private Bulgarian companies**. These present an attempt to apply the German model to coordinate interests of hired labor and owners through a dialogue and direct negotiations between employees and employers. This project seems to meet the moderate resistance of trade unions and in case such a practice spreads wider or measures are undertaken for its legal regulation, this might become another source of tension in industrial relations.

Another aspect of discord between trade unions and employers that will probably continue in future is related to **the drafts for significant amendments to the Labor Code proposed by employers**. These are aimed at further liberalization of the labor market in Bulgaria and in the end at reduction of unemployment. It is evident that hard and lengthy negotiations are to be held between the two parties and the government is expected to be the arbitrator.

Overall, 2002 can be defined as a year with no significant industrial conflicts and moderate social tension. Parallel to this there were periods and manifestations of active social discontent in the form of trade union protests (national and in individual sectors and enterprises) and protests by ethnic communities due to social and economic problems

The main topics discussed in 2002 in connection with health insurance were related to the amendments to the Health Insurance Act, the refusal by the Minister of Health to sign the Annex to the National Framework Agreement for 2002, the problems with the money for medications, which was depleted as early as the middle of 2002, and the amendments to the Human Medications and Pharmacies Act. It was not without a dispute, either, that the 2003 NHIF budget, which should ensure a higher standard of health care for the population in the next year, was adopted.

The International Monetary Fund has also expressed its concern about the delay in the health care reform and the healthcare indicators in Bulgaria, which are deteriorating unlike those of the other countries in transition. The main reason for the latter is that the available resources are not used efficiently. The hospital accreditation, which should determine which hospitals are qualified and possess the resources to deliver high quality medical care, is in delay. There is a delay also with the optimization of inefficient structures and that is why the health care funds are spent to meet current needs instead of making investments. The larger subsidies from the state budget will not be able to help improving the health care services quality, unless expenditures are made more rationally.

The discussions on the amendments to the Health Insurance Act opened several significant topics, which need resolution, as follows: the health care strategy and legislation in place, manufacturing, trading, and consumption of medications. Due to an oversight the new Health Insurance Act, which was promulgated in the Official Gazette in mid-November, had to be amended. According to the provision that caused the problem the parents of children of age up to 18 had to be refunded with the money, which they had paid for health insurance contributions. This was due to the omission in the passed Act to stipulate that it would enter into force on 1 January 2003 and after that date the state would undertake the payment of children's health insurance. According to data from the NSSI children of age up to 18 in Bulgaria amount to approximately 1.55 million, which means the state would have to pay BGN 0.85 per child, thus about BGN 1.320 million would have to be transferred to the NSSI only for the month of December.

Due to the process of amendments to the Health Insurance Act the signing of the 2003 National Health Agreement will happen only in March at the earliest. The delay in the signing of the Framework Agreement between the NHIF and the professional associations of medical doctors and dentists hindered the use of the funds allocated for health insurance payments.

In the middle of September the Bulgarian Medical Association jointly with the Dentists' Union filed a complaint with the Supreme Administrative Court against the tacit refusal by the

Minister of Health to re-sign the Annex to the 2002 National Health Agreement, which was supposed to provide additional funding for ensuring sufficient number of examinations in the out-patient specialized medical care, as well as a slight cost decrease in dentistry services. A three-member bench of the Supreme Administrative Court reversed the tacit refusal of the Minister of Health on the premise of the fact that the Minister had no power to assess the expediency of that Agreement. Despite the court's ruling, however, the Agreement could not be applied retrospectively and could have validity only if the signing of the new health care agreement for 2003 was delayed.

The latest possible date for entering into force of the National Framework Agreement for 2003 is 1 March 2003. The negotiations on the Health Agreement among the National Health Insurance Fund, the Bulgarian Medical Association and the Dentists' Association, which will be held in early 2003, will be based on the main package of health care activities that is guaranteed by the NHIF budget. The package includes 81 clinical paths, which cover approximately 1,500 diagnoses. The new groups of diseases, the treatment of which will be paid for by the NHIF, amount to about 50, such as surgical intervention, cancer and cardio-vascular diseases, etc. Under the 2002 National Framework Agreement the NHIF used to pay for 40 clinical paths covering a total of 485 diseases. It is expected that in 2003 the NHIF will cover between 70 and 100 per cent of the in-hospital treatment costs over the clinical paths, while by now it used to cover between 30 and 90 per cent of the different groups of diseases.

There is an intention to expand the treatment activities under the dentistry package for children of age up to 18 years. In the new 2003 the NHIF is expected to pay also for the treatment of the children living in social homes. Introduction of a one-time mandatory examination for taking the dental status of pregnant women is also planned.

The annual reserve destined for unexpected and urgent costs has already become 10 per cent of the collected health insurance contributions (over BGN 73 million for 2003), and the intention is that most of it be spent on medications because the amounts for medications expenditures were reduced upon the adoption of the NHIF budget to approximately BGN 163 million, while in 2002 that amount was about BGN 240 million.

The state achieved majority in the NHIF Representatives Assembly, which is the supreme body of this institution and elects the Managing Board and adopts the NHIF budget. The Government's quota has been increased to 18 people, while the employers, insured individuals and municipalities have only 6 representatives each. Thus the role of the state in the operations with the NHIF financial flows is practically increased.

Without any problems at all, the Rosche-Bollar rule was

introduced in the Human Medications and Pharmacies Act. This rule gives the Bulgarian manufacturers the opportunity to start preparing for registration of generic medications two years prior to the expiry of the patent protection of the original products, which means that the Bulgarian pharmaceutical manufacturers will be able to develop analogues and launch them on the market immediately after the patent of the originals expires. About the end of December the MPs introduced the so-called “data exclusivity”, which has direct impact on pharmaceutical manufacturers because it gives 6-year protection of the information in the medical dossier of each medication. The purpose is to protect the large pharmaceutical companies and to encourage them to spend funds on research and development.

The main reason for the deficit in the medications budget is **the lack of integrated information system and electronic medical dossier of the individuals having health insurance.** The contract with the US company *Aremissoft* was terminated. The project value was BGN 7.080 million and most of the money was given from the state budget; the NHIF paid the US company BGN 3.7 million for the finished modules. The balance of funds under the contract with *Aremissoft* is not sufficient for the purchase of standard software. The required funds will probably be supplemented from the taxpayers’ “pockets” because the NHIF budget contains no provision for such expenses. The World Bank is preparing a bidding procedure for audit of the work done by *Aremissoft* and to assess whether the modules submitted to the NHIF meet the requirements. It will become clear only after the audit whether options will be considered for further building-up of the system started by *Aremissoft*, or new ready-made software will be purchased. According to the Health Insurance Act the information system of the NHIF should be completed by the end of 2003, but this term seems quite optimistic. Without a well functioning information system the funds for medications will continue to be used inefficiently.

The health care problems will not be resolved in 2003 again, unless there is a well-functioning medications market, good legislation and institutions, well-operating information system of the NHIF and constructive negotiations for signing the new framework agreement between the representatives of the NHIF and the Medical and Dentists’ Associations.

Several focus points of 2002 Bulgarian environmental policy were outlined throughout the year. The successful development of the process of **harmonization of national legislation with that of the European Union** was of special importance for the progress of negotiations on Chapter 22: Environment. The passing of a new framework law - the Environment Protection Act, a new Biodiversity Act, of regulations on the application of the Chemicals Act and the Water Act was an important point in this field. Legislative activity resulted in harmonization of Bulgarian with EU practices related to environmental effect assessment procedures, prevention of industrial pollution, eco-labeling, introducing environment management systems in industrial enterprises, ensuring access to environmental information, application of the European directives concerning natural habitats and wild flora and fauna, trade in endangered species, etc. The progress achieved was given a positive assessment in the Commission's Regular Report on the Progress of Bulgaria towards Accession. The future evolution of this process will be dependable on the development of legislation in the field of genetically modified organisms, noise levels of machinery and equipment, waste management, prevention of pollution, clearness of air, environment protection, radiation protection, industrial pollution and risk control sectors.

Along with improvement of the regulatory basis in the field of environment protection, considerable progress was also achieved in **the implementation of basic environmental principles** in agriculture (by introducing and promoting the application of environmentally sound practices in agriculture) and in the energy policy field (by promoting the introduction of energy efficient techniques and technologies, introducing a set of measures to increase energy efficiency in industry and public services, developing a 2002-2010 National Program for Bulgarian Renewable Energy Sources).

Another focus point included **building, training, and strengthening of the institutional potential and the administrative capacity** for efficient application of environmental legislation and standards. The set up of four water basin management directorates (in the Danube region, the Black Sea, the East Aegean Sea and the West Aegean Sea regions) is a serious prerequisite for modern management of Bulgarian water resources in the context of the requirements of EU framework directive concerning water, for achieving good water quality and efficient use of water resources. Projects to improve the administrative capacity in the field of local level waste management, water basin management, and chemicals have been developed under the EU PHARE Program.

The past year was also characterized by efforts on the part of the Government institutions to lay the foundations of long-term beneficial cooperation with representatives of Bulgarian business. Cooperation which deserves support and mutually beneficial incentives, notwithstanding that results did not always meet expectations and partners's assessments of

its initial forms were often contradictory. Thirteen programs amounting to a total of BGN 200 million have been developed and are successfully implemented in relation to the morbid problem, from companies' point of view, concerning Government's obligations to remedy the damages of previous environmental pollutions before to the time of privatization. A Pilot Environment Improvement Program amounting to a total of around BGN 50 million has been successfully completed for the region of Pirdop.

Environmental standards incorporated in Bulgarian legislation in the course of its harmonization with the European legislation set strict requirements for **250 Bulgarian companies within the period 2002 - 2007 to create conditions for operation of existing industrial facilities** in accordance with the best available techniques, to improve energy efficiency of production and to reduce the quantity of raw materials and natural resources used.. These measures will be implemented employing the system of comprehensive permits. Thirteen pilot permits were issued in the past year to basic Bulgarian companies including Agropolychim AD, Devnia; Sviloza AD, Svishtov; Stomana Industry AD, Pernik; Sopharma AD, Sofia; Orgachim AD, Russe, etc., within a project financed by the World Bank. Another 72 comprehensive permits are to be issued in 2003.

National industry was engaged in environmental improvement by involvement in the National Environmental Management and Audit Scheme and the National Eco-labeling Scheme. Government's Strategy of Accelerated Negotiations for Bulgaria's Accession to the European Union sets forth organization of regular consultations with the industry sector on responsibilities and obligations related to the required investments for application of harmonized legislation.

Table 4. Monitoring of Negotiations for Bulgaria's Accession to EU

Chapter	Status (31 December, 2002)
1 Free Movement of Goods	Temporary closed
2 Free Movement of Persons	Temporary closed
3 Freedom to Provide Services	Temporary closed
4 Free Movement of Capital	Temporary closed
5 Company Law	Temporary closed
6 Competition Policy	Open
7 Agriculture	Open
8 Fishery	Temporary closed
9 Transport Policy	Open
10 Tax Policy	Temporary closed
11 Economic and Monetary Union	Temporary closed
12 Statistics	Temporary closed
13 Social Policy	Temporary closed
14 Energy	Temporary closed
15 Industrial Policy	Temporary closed
16 Small and Medium-Sized Enterprises	Temporary closed
17 Science and Research	Temporary closed
18 Education and Training	Temporary closed
19 Telecommunications	Temporary closed
20 Culture and Audiovision	Temporary closed
21 Regional Policy	Open
22 Environment	Open
23 Consumer Protection	Temporary closed
24 Justice and Home Affairs	Open
25 Customs Union	Temporary closed
26 Foreign Relations	Temporary closed
27 Common Foreign and Security Policy	Temporary closed
28 Fiscal Control	Temporary closed
29 Fiscal and Budgetary Issues	Open
30 Institutions	Temporary closed
Total chapters closed	23

Twenty-three chapters of the negotiations for Bulgaria's accession to EU were temporary closed in 2002. Bulgaria closed 6 chapters by the end of the Spanish Presidency (30 June 2002) and another 3 during the Danish Presidency (1 July – 31 December).

In the beginning of the year the Government adopted an **Accelerated EU Negotiations Strategy and a Communication Strategy**. On 13 May 2002 the Government approved the **2002-2006 Action Plan** and a **2002 Operational Program to the Communication Strategy for Preparation of Bulgaria's EU membership**. The Council of Ministers also approved the set up of a **Council on European Integration** to be charged with strategic planning, monitoring and performance assessment of the strategy, the action plan and the operational program. The objective of these documents is to coordinate and synchronize the actions of government institutions and non-government partners in coordination with the Communication Strategy approved on 24 January 2002.

At the end of May 2002, upon a proposal by the Prime Minister and by a resolution of the National Assembly the

Chief Negotiator for Bulgaria with the European Union was given the status of Minister on European Affairs who would directly participate in state government. Thereby the Deputy Minister of Foreign Affairs Meglena Kouneva became a minister in the present Government. The Minister on European Affairs will be assisted in her work by the Ministry of Foreign Affairs. The ministry raised the rank of the chief negotiator thereby underlining the importance Bulgaria attributes to its EU accession.

At the end of August 2002 the Government approved and adopted a **Pre-Accession Economic Program (2002-2005)**. The program is a general document reflecting mid-term objectives and priorities of Bulgarian society and proposing a reasonable and integrated method to achieve them in the period 2002-2005. It has been developed in accordance with the specific recommendations of the European Commission, adopted at the Madrid Summit of the Members of the Council of Member States Economic and Financial Ministers on 26 March 2002.

On 24 September 2002, the Minister on European Affairs Meglena Kouneva and the Minister of Energy and Energy Resources Milko Kovachev announced **Bulgaria's new official position on Kozloduy NPP**. The country would accept any request of the European Union to close down the two units, provided it is based on expert assessment of the condition of reactors. Bulgaria's position is that the European Union will have to prove by technical arguments that the units are dangerous and must be closed.

In November 2002, the European Union accepted the position of the Bulgarian Government and Chapter 14: Energy, was provisionally closed. This was made possible following presentation by the Bulgarian Government of additional information which states the year 2006 as a closing date for units 3 and 4 of Kozloduy NPP.

In 2002 Bulgaria also joined a couple of EU programs, including MEDIA PLUS, MEDIA-TRAINING (2000-2005), EC Program for Equality of Genders (2001-2005), EC Anti-Discrimination Program (2001-2006), EC Program to Fight Social Inequality (2002 -2006). Bulgaria also signed an agreement with the European Commission for association to the **Sixth Framework Program (2003-2006)** and declared its interest in association to the EurAtom Framework Program (2003-2006) for nuclear research.

The 2002 Regular Report of the Commission on the Progress of Bulgaria was published on 9 October 2002. It is stated for the first time that **Bulgaria is a functioning market economy**. The 2001 assessment classified Bulgaria as a country close to the functioning market economy.

November was important month for Bulgaria on its way to

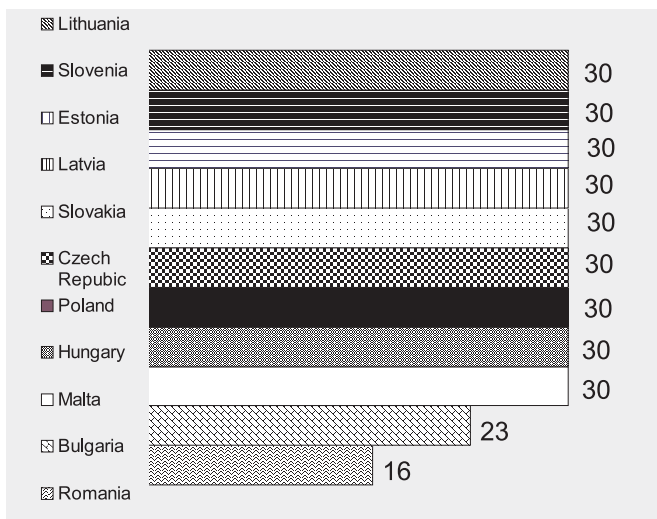
accession to the European Union and the other Euro-Atlantic structures. At the Prague Summit (21 November 2002) **Bulgaria received an official invitation for NATO membership.**

The year ended with good news from Copenhagen as well. **The European Council in Copenhagen (12-13 December 2002) adopted other important for Bulgaria decisions. Bulgaria and Romania will become EU members in 2007, provided they continue their progress in fulfilling membership criteria.** The Danish Presidency wanted to secure EU enlargement after 2004 (when the union will probably comprise 25 states) by engaging the countries of the first wave with the membership of Bulgaria, Romania, and Turkey.

The road maps presented by the European Commission set clear goals for Bulgaria and Romania and enable each country to determine its own pace in the process of accession. It is essential for the two countries to make use of this opportunity by accelerating their preparation, including in the fulfillment and implementation of the commitments undertaken in the negotiations for accession.

The Conclusions of the European Council in Copenhagen state that “finalization of the negotiations for accession with ten candidate countries accelerates the prospects for accession of Bulgaria and Romania as part of the same irreversible enlargement process”.

Figure 16. Temporary Closed Chapters of Negotiations for Accession (by candidate countries, as of 31 December, 2002)



In 2002 the Government launched specific initiatives for improving the business environment. The efforts were targeted at the following: alleviation of licensing regimes, regulating public procurement, fostering of competition, solving the problems with bankruptcy and liquidation, reform of the judicial system and fight against corruption. The work completed in the above mentioned areas was targeted at improving the business climate and more tangible results could be expected in the future.

The effect from the adopted measures is not unambiguous - entrepreneurs in general do not register considerable improvement of the business conditions.

In the last year we witnessed some very important events, which would have a positive impact on the business environment in a way of improving the certainty and stability of investors. We mean the recognition given to Bulgaria as a functioning market economy and the road map for accession to the EU, and the invitation to NATO membership. These two events are of considerable importance although their effect on the economy is not a direct and immediate one. In any case, however, these raise better certainty and confidence among the potential partners and investors in the country.

The agreements with the IMF (a two-year standby agreement reached at the end of 2001 and the agreement from the end of 2002), as well as the World Bank decision to grant the PAL loan (USD 150 million) that was passed in November should be added to the current list. Indisputably, these are facts that will have a positive impact on the business climate in the country.

Strategic and Program Documents. Economic Growth Council.

A number of documents have been adopted during the last year (strategies and programs) that are targeted at clearer outlining of some priorities, bringing more transparency and accomplishing a dialogue between the business and the state administration. The **Industry 2002 Program, the Fight against Corruption Strategy, Judicial System Reform Strategy and Program**, and others have been developed.

An Economic Growth Council has been established where the big employers' organizations have equal representation. This allowed them to have a regular and active dialogue and to solve jointly some business problems.

In October the government announced **a package of 9 legislative and structural measures for improvement of the business climate and enhancement of economic growth ("Vassilev" Program)**. These measures include: establishment of an investment fund with state participation; setting up of industrial zones; amendments to the Commercial Code in its section related to bankruptcy and liquidation;

resolving the problem of companies' mutual indebtedness; capital markets development; establishing a real estate market index; removing and simplifying licensing, permit and registration regimes; fostering the role of the Bulgarian Export Insurance Agency; taxation and social measures.

The announced measures are assessed differently by the business representatives and the experts. Some of the measures are perceived in connection with problems that will arise in the course of their implementation. Besides, most of the announced measures are tied to amendments in the regulations and adoption of new laws, which is time consuming and in reality many of these measures may be enforced only in the next year and later. However, those intentions may be estimated as positive ones, mostly as an expression of the trend towards improvement of the business conditions in the country and stimulation of the growth.

A number of legislation initiatives have been undertaken in the above mentioned areas.

Licensing Regimes

The Center for Economic Development surveys show that the licensing regimes are considered one of the main obstacles to the entrepreneurship growth. During the last year the Government adopted measures for alleviation of the administrative barriers. The licensing regimes reform started in the beginning of the year and is being carried out but at a slow pace. Unfortunately the problem with those regimes has not been solved yet.

According to the plans the reform had to take place in three stages. The first stage was completed to some extent in May 2002 when 74 regimes were repealed and another 120 regimes were eased. At the same time, however, a lot of new regimes have been introduced, many of them under the pretext that they are required by the process of harmonization with EU legislation.

The second stage provides for improving information exchange among all government structures related to the issuing of and control over licenses. The objective of those proposals is saving time and resources. The implementation of that second stage, however, is lagging behind.

The third stage provides for adoption of **Law on the Statutory Instruments and Administrative Proceedings** related to economic activities. It presumes the developing of common principles for enforcement of administrative procedures and bringing the operational and future regimes in conformity with those common principles.

Public Procurement

Amendments in the public procurement legislation have been implemented during the last year. The amendments were forced by the necessity of conforming with the EC positions and regulations, creating better conditions for fostering of competition and increasing the efficiency of the public procurement implementation.

The Act on Amendments to the Public Procurement Act was promulgated in the spring. In the beginning of June it was announced, however, that **the adoption of an entirely new Public Procurement Act is expected in 2003**. Such a step is forced by a number of reasons, the leading one being that the Bulgarian legislation should take into account two new EU directives related to public procurement that will be enforced in 2003. The amendments that are being considered are related to appeals against the procedures, relieving the terms of assigning public procurement orders by the utilities, looking for opportunities for introducing preferences for Bulgarian companies, and others.

The necessity for amendments of the legislation (the Public Procurement Act specifically) has been prompted by objective conditions. At the same time one of the main problems of the business environment, pointed out by the entrepreneurs, has been reiterated, namely the frequent amendments in the legislation.

Protection of Competition

The Act on Protection of Competition was amended last year. The main objective of the amendments was introduction of strict anti-cartel rules and strengthening the control over companies with dominant market position. The amendments provide for prohibition of agreements within amalgamations of companies; specifying the threshold of the so-called "insignificant effect agreements"; introducing the concept of malpractice with joint domination (the operation of two or more companies with joint dominant position is prohibited).

The powers of the Commission for Protection of Competition have been extended. It is entitled to enact the splitting of already established new companies or amalgamations, if they had been constituted in violation of the Act. The Commission is entitled to enforce the collection of evidence with judge's permission - a circumstance that may lead to racketeering and political pressure. The discussion of the proposals was accompanied by serious debates, mostly on the members of the Commission for Protection of Competition and how they are appointed. The extended powers of the Commission have been a source of disagreement. The Commission mandate expired on 10 December 2002 and the new members of the Commission have not been appointed yet.

State Aid

The State Aid Act and the Regulation and Ordinance for its Application have been adopted in 2002. The adoption of those documents was in reply to one of the main criticisms of EU to Bulgaria - the lack of control on granting state aid and lack of monitoring of its spending.

The documents regulate the limits of all state aid, state aid types, the role of the Commission for Protection of Competition as an agency, which permits the granting of state aid and determines the conditions and criteria that the grantee should meet.

Regulating the Bankruptcy Procedures

A draft for amendments to the Commercial Code in its section on bankruptcy and liquidation was drafted last year. The reform of the Commercial Code in its section on bankruptcy and liquidation aims at the introduction of fast and efficient bankruptcy procedures. The fast bankruptcy procedure is in the interest both of the debtors and creditors, as well as of the employees. In general terms those amendments mean drastic reduction of the procedures and shortening the terms for their execution, as well as improving the protection of the interests of the good-faith creditors.

The draft provides for amendments in the Company Law as well, giving more power to the shareholders and amending a number of details related to the holding of general meetings of shareholders and the majority required for adopting resolutions. A new chapter is added that regulates the procedures of merger, takeover, splitting, division, splitting to form a sole-proprietor company and others.

Judicial System and Fight against Corruption

The Regular Report of the EC about the progress of Bulgaria presented in October points out that Bulgaria should make further efforts for considerable strengthening of its judicial and law enforcement institutions. This is one of the areas where the country has been seriously criticized by a number of international institutions. An **Act on Amendments to the Judicial Power Act was developed and adopted** in response to this criticism and it received the approval of the international partners. The objective of the amendments is making the judiciary branch more transparent.

In September, however, the Supreme Court judges challenged at the Constitutional Court the amendments to the Act on the Judiciary proposed and adopted by the Parliament. This act will give rise to new arguments and obscurity regarding the direction of the judicial system reform. There were other serious concussions, scandals, arguments and contradictions in the judicial system at the end

of the year which confirmed the necessity of radical reforms in this field.

The problems that continue to create difficulties are: the clumsy procedure for investigating magistrates in breach because of their strengthened immunity, the lack of impartiality of the Supreme Judicial Council, the warring interests of the different sections of the judicial system and others. The majority in the Parliament declared its willingness to continue with the reforms in the judicial system. It was also proposed in December that a referendum about the necessity of such changes be held.

The assessments of the corruption incidence in the last year, made by different international and non-government organizations are not unambiguous. Generally, the problem with the corruption continues to exist.

A Strategy for the Fight against Corruption has been developed and a **Commission for Fighting Corruption** has been established at the Parliament, which started its work. The coordination of the different groups participating in the process, however, should be improved. The President's initiative for establishing a new agency, independent and equidistant from the other powers, for fighting against corruption has been announced in the beginning of 2003. Besides improving the legislation, the political will, the change in people's way of thinking and mentality are very important, too.

Administrative Reform and Support for the Business

In the middle of the year the Government adopted a **Strategy for Modernizing the State Administration: From Accession to Integration**, accompanied by implementation plan. The main objective of the Strategy is stimulating the state administration to show higher responsibility. This is the next one among a number of strategies for improving the efficiency of the state administration. It is difficult to say whether this Strategy will work, as it has some shortcomings - lack of good structure and continuity in the measures, uncertain issues related to the status of civil servants, and others.

The Government adopted a **Concept for Improving the One-Stop-Shop Service and "e-Government Strategy"** in the last year. The objective of such documents is to facilitate the citizens, businesses and public administration, to reduce the corruption sources and to save time and money. Those documents presume that all services will be provided through Internet. The Strategy envisages a minimum package of services provided through Internet to be introduced by 2005 - 12 services for the citizens and 8 services for the business.

A package of legislative measures for the introduction of e-Government has been developed, too.

ANNEX 1: MAIN INDICATORS FOR 2002

Economic dynamics													
Industry	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Year
Industrial production, volume index, previous month =100, %													
2002	86.5	118.8	114.9	104.5	99.1	104.2	106.3	97.2	108.4	101.6	111.7	106.1	-
2001	79.3	110.5	111.1	89.9	103.6	106.3	103.6	105.3	101.9	106.2	106.6	106.5	-
Industrial production, volume index, corresponding month of the previous year = 100, %													
2002	97.1	100.1	97.5	115.5	105.3	103	108.5	106	106.7	100.6	111	100.8	-
2001	93.5	128	102.1	101.6	104	100.2	106.8	110.3	102.7	99.3	101.3	95	-
Industrial production, from the beginning of the year, volume index, corresponding period of the previous year = 100, %													
2002	97.1	97.3	96.9	101.3	102.1	101.5	102.8	103.8	103.9	103.2	103.3	102.6	-
2001	93.5	111.9	102.5	103	102.4	101.7	102	102.6	102.2	101.5	102.4	100.7	-
Industrial sales, total, volume index, previous month =100, %													
2002	84	99.6	110	109.3	92.8	108.5	106.3	94.4	101.7	99.3	103.8	103.5	-
2001	80	103.5	105.4	90.3	105.4	100.5	101.7	99.8	97.1	106.8	97.6	101.9	-
Industrial sales, total, corresponding month of the previous year = 100, %													
2002	91.8	88	89.1	106.3	94.3	100.1	107.3	102.6	105.4	97.1	103.8	102.1	-
2001	112.8	105.7	99.8	104.3	103.9	97.4	102.3	99.1	95.4	96.7	92.8	92.7	-
Industrial sales, total, A43, volume index, corresponding period of the previous year = 100, %													
2002	91.8	90.3	89.4	93.8	94	94.5	96.9	97.6	98.7	98.5	99	99.8	-
2001	112.8	109.2	104.9	104.6	104.4	103.1	103.2	102.8	101.9	101.2	100.6	99.4	-
Domestic trade													
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Year
Trade and repairing activities, total, net receipts from sales, volume index, previous month =100, %													
2002	-	113.3	111.7	98.9	98.2	101.6	111.6	102.4	101.4	108.3	96.6	109.5	-
2001	-	101.7	118.3	90.3	103.3	99.2	111.2	100.9	90.7	102.7	95.3	115.4	-
Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, previous month =100, %													
2002	-	99.7	116.9	95.4	99.6	107.7	106.7	97	102.7	107.9	101.6	102.4	-
2001	-	91.9	125.6	87.8	107.3	104.8	102.7	104.2	90.3	99	97.9	118.2	-
Wholesale and commission trade, net receipts from sales, volume index, previous month =100, %													
2002	-	118.3	112	99.1	97.3	100.5	113.7	103	100.9	109.3	95.4	109.9	-
2001	-	104.2	119.8	89	101.6	98.4	114.9	99.6	88.8	104.3	94.1	114.8	-
Retail trade, repair of personal and household goods, net receipts from sales, volume index, previous month =100, %													
2002	-	100.8	106.4	100.1	101.7	102.6	105.1	103.3	102.9	103.7	99.6	112.6	-
2001	-	98.1	108	97.7	108.3	99.5	101.8	104.8	99	98.7	98.6	115.9	-
Trade and repairing activities, total, net receipts from sales, volume index, corresponding month of the previous year = 100, %													
2002	93.1	100.1	97.9	103	100.1	101.9	106.6	108.9	110.6	109.5	109	111.1	-
2001	95.1	99.2	101.1	102.7	105.4	100.3	102	102.4	95.9	95.6	96.4	98.8	-

ANNEX 1: MAIN INDICATORS FOR 2002

(continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, corresponding month of the previous year = 100, %																	
2002	97.3	106.7	103.1	103.1	98.4	98.5	98.7	98.9	101.4	102.9	105.3	104.7	-	-	-	-	-
2001	99.4	90.1	100.3	102.9	107.7	110.8	109.3	107.5	107.1	95.9	104.8	101.8	-	-	-	-	-
Wholesale and commission trade, net receipts from sales, volume index, corresponding month of the previous year = 100, %																	
2002	90.9	98.7	96.4	103.2	100.3	102.6	108.3	110.9	113.5	111.6	110.8	113.4	-	-	-	-	-
2001	92.0	100.2	101.4	102.1	104.6	98.3	99.8	100.4	92.4	93.9	93.7	97.2	-	-	-	-	-
Retail trade, repair of personal and household goods, net receipts from sales, volume index, corresponding month of the previous year = 100, %																	
2002	101	103.4	101.6	101.9	100.2	101.1	104.5	106.2	104.1	103.7	103.3	104.9	-	-	-	-	-
2001	107.8	101.0	100.7	105	107.2	101.7	107.7	107.8	104.7	103.1	103.5	103	-	-	-	-	-
Trade and repairing activities, total, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																	
2002	93.1	96.7	95.4	97.3	97.9	98.5	99.8	101	102.1	102.9	103.5	104.3	-	-	-	-	-
2001	95.1	96.6	98.2	101	101.9	101.6	101.6	101.7	101	100.6	100.2	100.1	-	-	-	-	-
Trade of motor vehicles and motorcycles, repair of motor; retail trade of automotive fuel, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																	
2002	97.3	101.8	102.3	102.5	101.6	101	100.7	100.4	100.5	100.8	101.3	101.7	-	-	-	-	-
2001	99.4	94.8	96.8	98.6	100.4	102.2	103.1	103.7	104.1	103.3	103.5	103.3	-	-	-	-	-
Wholesale and commission trade, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																	
2002	90.9	94.9	93.2	95.7	96.6	97.6	99.2	100.7	102.2	103.2	104	104.9	-	-	-	-	-
2001	92.0	95.1	97.5	100.7	101.5	100.9	100.7	100.6	99.7	99.1	98.6	98.5	-	-	-	-	-
Retail trade, repair of personal and household goods, net receipts from sales, volume index, from the beginning of the year, corresponding period of the previous year =100, %																	
2002	101	102.3	102.1	102.1	101.7	101.6	102	102.6	102.8	102.9	102.9	103.2	-	-	-	-	-
2001	107.8	104.3	102.8	103.9	104.7	104.1	104.6	105.1	105.1	105.3	105.1	104.9	-	-	-	-	-
Inflation																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Inflation (Consumer price index - 100), previous month =100, %																	
2002	2.7	1.6	0.8	-0.1	-2.1	-1.7	0.1	-0.7	0.8	1	0.2	1.2	-	-	-	-	-
2001	0.6	0.3	0.1	-0.2	0.1	-0.1	-0.2	0.3	1.3	1.7	0.2	0.6	-	-	-	-	-
Inflation (Consumer price index - 100), December of the previous year = 100, %																	
2002	2.7	4.4	5.2	5.1	2.9	1.1	1.2	0.6	1.4	2.4	2.5	3.8	-	-	-	-	-
2001	0.6	1	1	0.8	0.9	0.8	0.6	0.9	2.2	4	4.2	4.8	-	-	-	-	-
Inflation (Consumer price index - 100), corresponding period of the previous year = 100, %																	
2002	7.0	8.4	9.2	9.2	6.9	5.2	5.5	4.5	4.0	3.2	3.2	3.8	8.2	7.1	4.6	3.4	5.8
2001	9.3	8.5	8.9	9.8	9.7	9.4	8.5	5.7	4.7	5.2	4.6	4.8	8.9	9.6	6.3	4.9	7.4
Employment and unemployment																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Unemployed persons registered, total, end of the period, number																	
2002	687 805	683 894	668 972	678 637	673 803	659 032	663 329	650 018	644 718	644 298	624 946	602 524	668972	659032	644718	602524	602524
2001	708 729	713 761	704 691	707 793	678 528	654 008	643 528	637 831	629 866	637 348	656 976	662 260	704691	654008	629866	662260	662260

ANNEX 1: MAIN INDICATORS FOR 2002

(continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Unemployment (Employment Agency, ratio to the economically active population from the population census in 1992), end of the period, %																	
2002	17.99	17.89	17.5	17.75	17.63	17.24	17.09	17.00	16.86	16.85	16.35	15.76	17.50	17.24	16.86	15.76	15.76
2001	18.54	18.67	18.43	18.51	17.75	17.11	16.83	16.68	16.48	16.67	17.18	17.32	18.43	17.11	16.48	17.32	17.32
Unemployment (Employment Agency, ratio to the economically active population from the population census in 2001), end of the period, %																	
2002	18.57	18.46	18.06	18.32	18.19	17.79	17.64	17.55	17.4	17.39	16.87	16.27	18.06	17.79	17.4	16.27	16.27
2001	19.13	19.27	19.02	19.11	18.32	17.66	17.37	17.22	17	17.21	17.74	17.88	19.02	17.66	17.00	17.88	17.88
Newly opened vacant jobs, end of the period, number																	
2002	1 588	4 177	3 284	3 420	2 437	2 055	2 011	3 272	2 802	2 270	2 651	1 926	3 284	2 055	2 802	1 926	1 926
2001	2 587	2 908	3 903	2 287	3 732	4 236	2 210	2 170	2 246	2 212	1 569	1 268	3 903	4 236	2 246	1 268	1 268
Employed person, total, average for the period, number																	
2002	1 878 628	1 883 392	1 890 173	1 895 911	1 905 823	1 913 121	1 917 999	1 914 477	1 925 092	1 917 214	1 918 643	1 911 216	1 884 064	1 904 952	1 919 189	1 915 691	1 905 974
2001	1 851 914	1 854 770	1 866 572	1 881 996	1 904 129	1 916 922	1 901 499	1 890 120	1 896 077	1 912 239	1 903 452	1 878 849	1 857 752	1 901 016	1 895 899	1 898 180	1 888 212
Employed person, public sector, average for the period, number																	
2002	761 630	762 192	760 562	749 826	745 729	743 092	737 200	735 424	740 543	735 825	747 422	756 733	761 461	746 216	737 722	746 660	748 015
2001	803 322	804 038	802 894	782 409	781 331	778 545	770 832	765 341	767 022	766 079	769 087	768 207	803 418	780 762	767 732	767 791	779 926
Employed person, private sector, average for the period, number																	
2002	1 116 998	1 121 200	1 129 611	1 146 085	1 160 094	1 170 029	1 180 799	1 179 053	1 184 549	1 181 389	1 171 221	1 154 483	1 122 603	1 158 736	1 181 467	1 169 031	1 157 959
2001	1 048 592	1 050 732	1 063 678	1 099 587	1 122 798	1 138 377	1 130 667	1 124 779	1 129 055	1 146 160	1 134 365	1 110 642	1 054 334	1 120 254	1 128 167	1 130 389	1 108 286
Fiscal review																	
State budget																	
	I	I-II	I-III	I-IV	I-V	I-VI	I-VII	I-VIII	I-IX	I-X	I-XI	I-XII	Q1	Q2	Q3	Q4	Year
Revenues of the Consolidated State Budget, total, BGN million																	
2002	889.1	1 752.7	2 782.3	4 040.8	5 156.1	6 064.4	7 247.7	8 194.7	9 180.6	10 312.3	11 315.3	12 524.8	2 782.3	3 282.1	3 116.2	3 344.2	12 524.8
2001	852.2	1 605.4	2 775.9	4 017.6	5 107.0	6 062.1	7 066.5	7 897.7	8 705.3	9 708.8	10 617.7	11 837.9	2 775.9	3 286.2	2 643.2	3 132.6	11 837.9
Expenditures of the Consolidated State Budget, total, BGN million																	
2002	1 020.3	1 905.9	2 821.1	3 928.6	4 816.5	5 733.6	6 843.6	7 778.0	8 688.8	9 667.1	10 789.5	12 743.1	2 821.1	2 912.5	2 955.2	4 054.3	12 743.1
2001	1 091.8	1 968.8	2 897.2	3 901.0	4 888.5	5 895.1	7 116.1	7 979.0	8 846.9	9 709.1	10 620.7	12 093.1	2 897.2	2 997.9	2 951.8	3 246.2	12 093.1
Consolidated State Budget deficit (-) /surplus (+), BGN million																	
2002	-131.2	-153.2	-38.8	112.2	339.6	330.8	404.1	416.7	491.8	645.2	525.8	-218.3	-38.8	369.6	161.0	-710.1	-218.3
2001	-239.6	-363.4	-121.2	116.6	218.6	167	-49.6	-81.3	-141.6	-0.3	-3	-255.2	-121.2	288.2	-308.6	-113.6	-255.2
Revenues of the Republican Budget, total, BGN million																	
2002	521.9	985.5	1 585.0	2 364.3	3 042.6	3 540.5	4 242.3	4 783.1	5 355.4	6 076.4	6 647.0	7 289.4	1 585.0	1 955.5	1 814.9	1 934.0	7 289.4
2001	462.5	872.5	1 550.6	2 258.5	2 879.4	3 358.3	3 884.4	4 334.9	4 764.0	5 322.4	5 816.6	6 525.9	1 550.6	1 807.7	1 405.7	1 761.9	6 525.9
Expenditures of the Republican Budget, total, BGN million																	
2002	367.7	869.5	1 376.1	2 113.1	2 531.4	3 018.5	3 718.5	4 205.2	4 697.0	5 252.8	5 949.2	7 286.0	1 376.1	1 642.4	1 678.5	2 589.0	7 286.0
2001	832.5	1 294.6	1 774.1	2 356.6	2 898.0	3 524.7	4 332.2	4 803.8	5 319.5	5 732.0	6 225.0	7 186.0	1 774.1	1 750.6	1 794.8	1 866.5	7 186.0

ANNEX 1: MAIN INDICATORS FOR 2002

(continued)

	I	I-II	I-III	I-IV	I-V	I-VI	I-VII	I-VIII	I-IX	I-X	I-XI	I-XII	Q1	Q2	Q3	Q4	Year
Republican Budget cash deficit (-) / surplus (+), BGN million																	
2002	154.2	116	208.9	251.3	511.1	521.9	523.8	577.9	658.4	823.5	697.8	3.4	208.9	313.0	136.5	-655.0	3.4
2001	-370	-422.1	-223.5	-98.1	-18.5	-166.5	-447.8	-468.9	-555.4	-409.6	-408.3	-660.2	-223.5	57.0	-388.9	-104.8	-660.2
Government and government guaranteed debt																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Government and government guaranteed debt, BGN million																	
2002	20 993	20 917	20 859	20 103	19 502	18 855	18 993	18 964	18 929	18 667	18 627	18 180	20 859	18 855	18 929	18 180	18 180
2001	20 486	20 458	21 058	20 612	21 610	21 797	21 198	20 367	19 846	20 041	20 709	20 752	21 058	21 797	19 846	20 752	20 752
Domestic government and government guaranteed debt, BGN million																	
2002	1 897	1 890	1 917	1 927	1 908	1 949	1 973	1 988	2 030	2 042	2 088	2 112	1 917	1 949	2 030	2 112	2 112
2001	1 717	1 706	1 743	1 733	1 752	1 767	1 769	1 738	1 767	1 813	1 821	1 861	1 743	1 767	1 767	1 861	1 861
Foreign government and government guaranteed debt, BGN million																	
2002	19 096	19 027	18 942	18 177	17 594	16 906	17 020	16 976	16 899	16 625	16 539	16 069	18 942	16 906	16 899	16 069	16 069
2001	18 769	18 752	19 315	18 879	19 859	20 030	19 429	18 630	18 080	18 228	18 888	18 892	19 315	20 030	18 080	18 892	18 892
Government and government guaranteed debt, ratio to the annual GDP, %																	
2002	68.2	68	67.6	65.3	63.4	61.3	61.8	61.6	61.5	60.6	60.5	56	67.8	61.3	61.5	56.0	56.0
2001	72.6	72.5	74.7	73.1	76.6	77.3	75.1	72.2	70.4	71	73.4	73.6	74.7	77.3	70.4	73.6	73.6
Domestic government and government guaranteed debt, ratio to the annual GDP, %																	
2002	6.2	6.1	6.2	6.3	6.2	6.3	6.4	6.5	6.6	6.6	6.8	6.5	6.2	6.3	6.6	6.5	6.5
2001	6.1	6	6.2	6.2	6.2	6.3	6.3	6.2	6.3	6.4	6.5	6.6	6.2	6.3	6.3	6.6	6.6
Foreign government and government guaranteed debt, ratio to the annual GDP, %																	
2002	62	61.8	61.4	59	57.2	55	55.4	55.2	54.9	54	53.7	49.5	61.5	54.9	54.9	49.5	49.5
2001	66.5	66.5	68.5	66.9	70.4	71	68.9	66	64.1	64.6	67	67	68.5	71.0	64.1	67.0	67.0
Domestic government debt, total, BGN million																	
2002	1 891	1 884	1 912	1 922	1 903	1 945	1 973	1 988	2 027	2 039	2 085	2 110	1 912	1 945	2 027	2 110	2 110
2001	4 176	4 148	4 371	1 724	1 742	1 758	1 760	1 730	1 759	1 806	1 814	1 854	4 371	1 758	1 759	1 854	1 854
Debt on Government Securities issued for budget deficit financing, BGN million																	
2002	1 144	1 139	1 172	1 198	1 201	1 269	1 286	1 307	1 351	1 369	1 418	1 462	1 172	1 268	1 351	1 462	1 462
2001	932	931	947	943	923	941	966	968	997	1 042	1 042	1 077	946	941	997	1 077	1 077
Debt on Government Securities issued for structural reform, BGN million																	
2002	746	745	740	724	702	677	684	677	676	670	667	648	740	677	675.9	648	648
2001	770	766	796	740	820	816	795	763	763	764	772	777	796	816	762.8	777	777
Domestic government guarantees, BGN million																	
2002	6.4	6	5.6	5.1	4.5	3.9	3.7	3.3	3	2.6	2.3	1.9	6.0	4.0	3.0	1.9	1.9
2001	9.7	9.5	9.7	9.2	9.5	9.2	8.6	7.8	7.5	7.2	7	6.7	10.0	9.0	7.5	6.7	6.7
Foreign government debt, USD million																	
2002	7 925	7 921	7 921	7 840	7 936	8 103	7 997	7 997	7 967	7 849	7 862	7 978	7 920	8 096	7 967	7 978	7 978
2001	8 472	8 421	8 290	8 275	8 145	8 187	8 176	8 221	7 942	7 931	8 103	8 006	8 290	8 187	7 942	8 006	8 006

ANNEX 1: MAIN INDICATORS FOR 2002

(continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Foreign government guaranteed debt, USD million																	
2002	508	496	503	505	509	529	524	538	541	536	533	546	529	526	541	546	546
2001	446	446	433	434	465	497	503	502	499	496	490	507	433	497	499	507	507
Foreign economic relations and foreign investments																	
Balance of Payments																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Current account, USD million																	
2002	-130.2	-49.7	-54.9	-136.9	-100.5	97.8	116.3	160.7	51.3	-139.1	-179.3	-314.1	-234.8	-139.6	328.3	-632.5	-678.6
2001	-136.4	-38.6	-46.1	-77.8	-89.7	-1.6	-74.8	84	-46	-114.1	-155.6	-145.5	-221.1	-169.1	-36.8	-415.2	-842.2
Exports (FOB), USD million																	
2002	383.6	408.7	407.9	425.4	402.9	496.3	586.2	525.4	527.6	514.8	517.4	381.9	1 200.2	1 324.6	1 639.2	1 414.1	5 578.1
2001	397.2	429.4	455.7	412.5	391.8	429.2	454.3	447.9	424.6	454.7	451.7	363.8	1 282.3	1 233.5	1 326.8	1 270.2	5 112.8
Imports (FOB), USD million																	
2002	465.8	482.2	501.7	573.5	591.9	565.7	668.4	581.8	609.1	693.6	732.9	730.4	1 449.7	1 731.1	1 859.3	2 156.9	7 197.0
2001	476.8	474.6	554.5	531.2	555.9	598.9	658.5	550.6	507.1	632.6	615.3	537.4	1 505.9	1 686.0	1 716.2	1 785.3	6 693.4
Trade balance, (FOB), USD million																	
2002	-82.2	-73.5	-93.8	-148.1	-189	-69.4	-82.2	-56.4	-81.5	-178.8	-215.5	-348.5	-249.5	-406.5	-220.1	-742.8	-1 618.9
2001	-79.5	-45.2	-98.8	-118.7	-164.1	-169.6	-204.3	-102.7	-82.5	-177.9	-163.6	-173.6	-223.5	-452.4	-389.5	-515.1	-1 580.5
Capital account, USD million																	
2002	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
2001	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Financial account, USD million																	
2002	-5.1	44.1	124.4	323.3	237.8	138.7	38.2	-83	113.9	272.7	159.9	188.5	163.4	699.8	69.1	621.1	1 553.4
2001	-36.1	52.8	-175.2	186.8	85.9	143.3	104.3	-56.5	106.3	267.1	511.9	-62.3	-160.5	416.0	154.1	716.7	1 126.3
Direct investment in Bulgaria, USD million																	
2002	20.3	29.7	72.2	86	37.5	-14.9	-23.5	23.4	24.1	110.1	40.3	52.8	122.2	108.6	24.0	203.2	458.0
2001	183.7	69.8	58	40.9	21.6	69.7	70	36.5	33.8	6.6	99.6	122.7	311.5	132.2	140.3	228.9	812.9
Finance																	
Financial indicators																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Exchange rate BGN / USD, average for the period																	
2002	2.21474	2.24804	2.23369	2.20959	2.13121	2.04781	1.97152	2.00039	1.99537	1.99354	1.95327	1.92447	2.23216	2.12954	1.98909	1.95709	2.07697
2001	2.0848	2.1223	2.15127	2.19193	2.23394	2.29254	2.27299	2.17258	2.14128	2.15933	2.20198	2.19164	2.11946	2.23947	2.19562	2.18432	2.18472
Exchange rate BGN / USD, end of the period																	
2002	2.26448	2.26081	2.2419	2.17121	2.08355	1.96073	1.99921	1.98905	1.9836	1.9828	1.97021	1.88496	2.24190	1.96073	1.98360	1.88496	1.88496
2001	2.10463	2.11487	2.21448	2.16761	2.3064	2.3064	2.23396	2.13565	2.14197	2.16305	2.19806	2.21926	2.21448	2.30640	2.14197	2.21926	2.21926
Basic interest rate, effective annual, for the period																	
2002	4.86	4.66	4.52	4.16	3.98	3.79	3.72	3.82	3.81	3.76	3.76	3.39	4.52	3.79	3.81	3.39	3.39
2001	4.49	4.17	4.23	4.35	4.5	4.55	4.58	4.76	4.81	4.72	4.77	4.75	4.23	4.55	4.81	4.75	4.75

ANNEX 1: MAIN INDICATORS FOR 2002

(continued)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Money (M1), BGN million																	
2002	4 651.4	4 584.3	4 594.2	4 602.9	4 474.8	4 402.9	4 589.0	4 750.4	4 804.9	4 804.1	4 936.0	5 542.7	4594.2	4402.9	4804.9	5542.7	5542.7
2001	3 962.3	3 978.9	4 010.9	4 128.2	4 135.7	4 039.2	4 163.9	4 193.7	4 275.1	4 240.9	4 982.0	4 883.8	4010.9	4039.2	4275.1	4883.8	4883.8
Money (M2), BGN million																	
2002	12 035.3	12 068.5	12 088.1	12 136.0	11 902.6	11 875.7	12 243.5	12 521.5	12 589.7	12 703.6	12 929.4	13 581.3	12088.1	11875.7	12589.7	13581.3	13581.3
2001	9 776.1	9 863.9	9 977.4	9 662.0	9 934.7	10 208.2	10 548.8	10 682.9	10 887.3	10 941.1	11 167.0	12 100.8	9977.4	10208.2	10887.3	12100.8	12100.8
International reserves of BNB, BGN million																	
2002	7 372.4	7 373.0	7 196.2	7 427.8	7 546.3	7 908.4	8 034.3	8 231.8	8 496.2	8 750.6	8 923.6	8 947.5	7196.2	7908.4	8496.2	8947.5	8947.5
2001	6 889.5	6 820.3	6 820.0	6 862.6	6 939.2	7 010.7	6 802.7	6 687.8	6 683.4	6 986.5	7 703.4	7 945.6	6820.0	7010.7	6683.4	7945.6	7945.6
Fiscal reserves at the Issue Department of BNB, BGN million																	
2002	2 276.2	2 260.4	2 106.5	2 358.9	2 803.3	3 020.8	3 065.5	3 108.2	3 238.9	3 482.0	3 685.8	3 034.7	2106.5	3020.8	3238.9	3034.7	3034.7
2001	2 389.9	2 260.4	2 329.1	2 878.9	2 863.9	2 925.3	2 418.6	2 304.3	2 129.4	2 440.4	2 913.2	2 571.2	2329.1	2925.3	2129.4	2571.2	2571.2
Banking system																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Credits granted to non-financial institutions and other customers, total, end of the period, BGN thousand																	
2002	4 226 013	4 267 336	4 354 165	4 527 779	4 651 472	4 769 243	5 047 813	5 179 755	5 414 813	5 553 525	5 740 939	6 033 915	4354165	4769243	5414813	6033915	6033915
2001	3 040 998	3 037 279	3 169 673	3 285 333	3 383 689	3 426 012	3 519 280	3 601 196	3 808 035	3 994 028	4 143 907	4 145 865	3169673	3426012	3808035	4145865	4145865
Credits granted to the budget, end of the period, BGN thousand																	
2002	5 505	6 739	7 291	7 031	7 314	6 871	6 564	9 494	9 601	9 583	9 694	8 680	7291	6871	9601	8680	8680
2001	3 396	5 199	5 870	5 042	4 707	4 023	4 195	4 648	91 972	145 710	149 712	5 772	5870	4023	91972	5772	5772
Credits granted to state owned companies, end of the period, BGN thousand																	
2002	164 898	156 145	161 650	201 201	203 441	193 604	193 793	195 258	183 275	192 726	193 796	203 362	161650	193604	183275	203362	203362
2001	111 436	118 284	122 139	121 285	122 095	130 020	140 881	128 437	121 422	120 827	117 572	148 273	122139	130020	121422	148273	148273
Credits granted to private companies, end of the period, BGN thousand																	
2002	3 220 930	3 255 827	3 312 957	3 409 601	3 508 806	3 601 207	3 838 302	3 923 562	4 125 524	4 210 382	4 356 167	4 612 569	3312957	3601207	4125524	4612569	4612569
2001	2 360 768	2 343 920	2 434 243	2 518 381	2 582 162	2 586 954	2 640 167	2 709 482	2 818 212	2 926 183	3 055 534	3 159 490	2434243	2586954	2818212	3159490	3159490
Credits granted to individuals and households, end of the period, BGN thousand																	
2002	834 680	848 625	872 267	909 946	931 911	967 561	1 009 154	1 051 441	1 096 413	1 140 834	1 181 282	1 209 304	872267	967561	1096413	1209304	1209304
2001	565 398	569 876	607 421	640 625	674 725	705 015	734 037	758 629	776 429	801 308	821 089	832 330	607421	705015	776429	832330	832330
Credits granted to the budget, % of the total																	
2002	0.13	0.16	0.17	0.16	0.16	0.14	0.13	0.18	0.18	0.17	0.17	0.14	0.17	0.14	0.18	0.14	0.14
2001	0.11	0.17	0.19	0.15	0.14	0.12	0.12	0.13	2.42	3.65	3.61	0.14	0.19	0.12	2.42	0.14	0.14
Credits granted to state owned companies, % of the total																	
2002	3.90	3.66	3.71	4.44	4.37	4.06	3.84	3.77	3.38	3.47	3.38	3.37	3.71	4.06	3.38	3.37	3.37
2001	3.66	3.89	3.85	3.69	3.61	3.80	4.00	3.57	3.19	3.03	2.84	3.58	3.85	3.80	3.19	3.58	3.58

ANNEX 1: MAIN INDICATORS FOR 2002

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Credits granted to private companies, % of the total																	
2002	76.22	76.30	76.09	75.30	75.43	75.51	76.04	75.75	76.19	75.81	75.88	76.44	76.09	75.51	76.19	76.44	76.44
2001	77.63	77.17	76.80	76.66	76.31	75.51	75.02	75.24	74.01	73.26	73.74	76.21	76.80	75.51	74.01	76.21	76.21
Credits granted to individuals and households, % of the total																	
2002	19.75	19.89	20.03	20.10	20.03	20.29	19.99	20.30	20.25	20.54	20.58	20.04	20.03	20.29	20.25	20.04	20.04
2001	18.59	18.76	19.16	19.50	19.94	20.58	20.86	21.07	20.39	20.06	19.81	20.08	19.16	20.58	20.39	20.08	20.08
Total assets, end of the period, BGN thousand																	
2002	12 340 044	12 286 166	12 710 381	12 722 090	12 473 976	12 394 798	12 924 968	13 225 015	13 475 455	13 503 015	13 901 329	14 557 124	12 710 381	12 394 798	13 475 455	14 557 124	14 557 124
2001	10 030 490	10 009 095	10 793 278	10 421 043	10 951 545	11 103 981	11 156 644	11 199 882	11 440 501	11 411 506	11 545 701	12 220 529	10 793 278	11 103 981	11 440 501	12 220 529	12 220 529
Total liabilities , end of the period, BGN thousand																	
2002	10 676 646	10 602 225	11 014 662	11 040 181	10 782 330	10 682 602	11 197 870	11 455 975	11 681 572	11 674 854	12 053 348	12 621 459	11 014 662	10 682 602	11 681 572	12 621 459	12 621 459
2001	8 510 363	8 470 980	9 143 456	8 731 672	9 462 114	9 609 537	9 623 763	9 640 825	9 878 415	9 819 659	9 937 092	10 565 823	9 143 456	9 609 537	9 878 415	10 565 823	10 565 823
Interest revenues, BGN thousand																	
2002	56 711	110 773	168 685	224 465	283 518	342 850	405 735	468 644	533 137	600 091	672 166	738 092	168 685	342 850	533 137	738 092	738 092
2001	55 742	107 205	163 567	220 524	279 833	336 002	395 993	453 631	509 521	568 718	625 241	686 760	163 567	336 002	509 521	686 760	686 760
Current profit/loss, BGN thousand																	
2002	25 913	47 270	56 996	80 116	112 082	132 715	148 229	182 185	201 740	240 089	258 199	266 625	56 996	132 715	201 740	266 625	266 625
2001	25 980	43 653	157 588	183 083	197 758	203 302	229 939	255 411	274 876	292 643	309 412	319 375	157 588	203 302	274 876	319 375	319 375
Social policy and industrial relations																	
Wage&Salary 1)																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Average Monthly Wage&Salary of employees under labor contract, total, nominal, BGN																	
2002	251	252	265	262	269	265	267	265	272	271	272	282	256	265	268	275	266
2001	231	228	239	248	254	254	249	248	256	253	255	270	233	252	251	259	249
Average Monthly Wage&Salary of employees under labor contract, public sector, nominal, BGN																	
2002	282	285	304	298	318	311	309	312	328	321	319	332	290	309	316	324	310
2001	257	254	271	281	300	295	287	284	307	287	293	316	261	292	293	299	286
Average Monthly Wage&Salary of employees under labor contract, private sector, nominal, BGN																	
2002	229	229	238	238	236	235	240	236	237	240	241	249	232	236	238	243	237
2001	211	208	214	223	222	225	222	224	221	230	229	238	211	223	222	232	222
Real Average Monthly Wage&Salary of employees under labor contract, total, growth, corresponding period of the previous year =100, %																	
2002	1.6	2.0	1.6	-3.3	-0.9	-0.8	1.6	2.3	2.2	3.8	3.4	0.6	1.7	-1.7	2.0	2.5	1.1
2001	6.2	3.5	1.2	3.6	2.9	4.1	2.9	5.7	4.1	7.4	4.2	4.7	3.6	3.5	4.2	5.4	4.2
Real Average Monthly Wage&Salary of employees under labor contract, public sector, growth, corresponding period of the previous year =100, %																	
2002	2.6	3.5	2.8	-2.9	-0.8	0.2	2.1	5.2	2.8	8.3	5.5	1.2	3.0	-1.2	3.3	4.9	2.4
2001	6.4	5.5	2.4	4.9	6.0	7.5	6.7	8.8	7.8	10.0	5.3	5.8	4.7	6.1	7.7	6.9	6.4

ANNEX 1: MAIN INDICATORS FOR 2002

(continued and end)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Real Average Monthly Wage&Salary of employees under labor contract, private sector, growth, corresponding period of the previous year =100, %																	
2002	1.4	1.6	1.9	-2.3	-0.6	-0.7	2.5	0.8	3.1	1.1	2.0	0.8	1.6	-1.2	2.2	1.3	0.9
2001	7.8	3.6	2.4	4.1	3.2	3.4	1.3	4.9	3.0	6.1	4.7	5.6	4.6	3.6	3.1	5.5	4.2
Income and consumption of the households 1)																	
	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII	Q1	Q2	Q3	Q4	Year
Total income, monthly, average per person, nominal, BGN																	
2002	113.4	113.2	126.5	130.6	136.6	135.3	137.3	142.7	148.5	146.7	144.1	195.5	117.7	134.2	142.8	162.1	139.2
2001	105.9	99.2	112.2	117.6	122.3	122.3	123.8	125.9	126.8	126.1	126.8	152.6	105.8	120.7	125.5	135.2	121.8
Cash income, monthly, average per person, nominal, BGN																	
2002	109.3	109.6	120.9	122.0	123.1	123.5	124.8	128.7	135.5	132.2	126.3	157.0	113.3	122.9	129.6	138.5	126.1
2001	101.6	96.1	106.8	109.0	111.0	111.8	112.3	113.5	114.8	114.2	112.1	125.7	101.5	110.6	113.5	117.3	110.7
Total expenditure, monthly, average per person, nominal, BGN																	
2002	109.4	112.0	120.3	124.1	136.4	130.6	133.6	140.8	147.6	143.6	141.6	183.8	113.9	130.4	140.7	156.3	135.3
2001	104.9	95.4	107.1	113.9	121.2	115.3	120.0	122.7	126.4	124.8	122.0	147.3	102.5	116.8	123.0	131.4	118.4
Cash expenditure, monthly, average per person, nominal, BGN																	
2002	105.5	108.6	114.9	115.6	123.2	118.9	121.2	127.0	134.9	129.8	124.2	146.3	109.7	119.3	127.7	133.4	122.5
2001	100.7	92.4	101.8	105.4	110.3	104.9	108.5	110.6	114.5	113.1	107.4	120.6	98.3	106.9	111.2	113.7	107.5
Real total income, monthly, average per person, growth, corresponding period of the previous year =100, %																	
2002	0.1	5.3	3.3	1.7	4.5	5.2	5.2	8.5	12.6	12.7	10.2	23.4	2.9	3.8	8.8	16.0	8.0
2001	-4.6	-2.9	-1.9	-2.3	-1.2	-0.5	-7.3	0.6	-1.4	-1.4	-4.4	-15.0	-2.5	1.0	-1.3	-6.6	-2.7
Real cash income, monthly, average per person, growth, corresponding period of the previous year =100, %																	
2002	0.6	5.2	3.7	2.5	3.8	5.0	5.3	8.5	13.5	12.1	9.2	20.3	3.2	3.7	9.1	14.2	7.6
2001	-4.5	-2.2	-1.3	-1.0	-0.3	0.6	-6.8	2.5	0.2	-0.1	-2.2	-14.7	-2.0	2.1	0.1	-5.1	-1.5
Real total expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %																	
2002	-2.5	8.3	2.9	-0.3	5.3	7.7	5.5	9.8	12.3	11.5	12.5	20.2	2.8	4.2	9.3	15.1	8.0
2001	0.3	-7.3	-5.1	-2.7	-1.6	-2.2	-5.1	-2.5	-2.4	-2.9	-6.0	-10.7	-3.4	0.1	-1.9	-5.6	-3.0
Real cash expenditure, monthly, average per person, growth, corresponding period of the previous year =100, %																	
2002	-2.1	8.5	3.4	0.4	4.5	7.8	5.9	9.9	13.3	11.2	12.1	16.9	3.1	4.2	9.7	13.5	7.7
2001	0.6	-6.8	-4.6	-1.6	-0.9	-1.2	-4.3	-1.0	-1.0	-1.8	-4.1	-9.3	-3.0	1.1	-0.6	-3.9	-1.8

1) Average monthly values by quarters and years are calculated as simple average of monthly values.

Sources: Employment Agency, Bulgarian national bank, Ministry of finance, National statistical institute and own calculations.

Acronyms:

GDP = Gross domestic product

"-" = Not applicable or missing data

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